Supreme Ct.

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NO. _____

IN THE

Supreme Court of the United States

TIME WARNER ENTERTAINMENT COMPANY, L.P., *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION AND
UNITED STATES OF AMERICA,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITIONERS' APPENDIX
Volume I Pages 1-181

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App. 1

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

Argued October 17, 2000 Decided March 2, 2001

No. 94-1035

TIME WARNER ENTERTAINMENT CO., L.P.

PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION AND

UNITED STATES OF AMERICA,

RESPONDENTS

BELLSOUTH CORPORATION, ET AL.,

INTERVENORS

Consolidated with

95-1337, 99-1503, 99-1504, 99-1522,

99-1541, 99-1542, 00-1086

On Petitions for Review of Orders of the

Federal Communications Commission

David W. Carpenter argued the cause for petitioners AT&T Corporation and Time Warner Entertainment Co., L.P. With him on the briefs were *Peter Keisler, David L. Lawson, C. Frederick Beckner III, Henk Brands* and *Robert D. Joffe. Charles S. Walsh, Richard B Beckner, Stuart W. Gold* and *Marc C. Rosenblum* entered appearances.

Robert D. Joffe and *Henk Brands* were on the briefs for petitioner Time Warner Entertainment Co., L.P. *Charles S. Walsh, Richard B. Beckner* and *Stuart W. Gold* entered appearances.

Andrew Jay Schwartzman, Cheryl A. Leanza and *Harold Feld* were on the briefs for petitioner Consumers Union.

James M. Carr, Counsel, Federal Communications Com- mission, argued the cause for respondents. With him on the brief were *Christopher J. Wright*, General Counsel, *Daniel M. Armstrong*, Associate General Counsel, *Joel Marcus* and *James M. Carr*, Counsel, *David W. Ogden*, Acting Assistant Attorney General, U.S. Department of Justice, *Mark*

B. Stern and *Jacob M. Lewis*, Attorneys, and *Wilma A. Lewis*, U.S. Attorney. *William E. Kennard*, General Counsel, Federal Communications Commission, *John E. Ingle*, Deputy Associate General Counsel, and *Catherine G. O'Sullivan*, *Robert B. Nicholson* and *Robert J. Wiggers*, Attorneys, U.S. Department of Justice, entered appearances.

Henk J. Brands, *Robert D. Joffe*, *Peter D. Keisler*, *David L. Lawson* and *C. Frederick Beckner III* were on the brief for intervenor Time Warner Entertainment Co., L.P. in No. 99-1522. *Mark C. Rosenblum* entered an appearance.

Before: WILLIAMS, RANDOLPH and TATEL, *Circuit Judges*.

Opinion for the Court filed by *Circuit Judge* WILLIAMS.

WILLIAMS, *Circuit Judge*: Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 ("1992 Cable Act"), amends 47 U.S.C. § 533 to direct the Federal Communications Commission to set two types of limits on cable operators. The first type is horizontal, addressing operators' scale: "limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest." 47 U.S.C. § 533(f)(a)(1)(A). The second type is vertical, addressing operators' integration with "programmers" (suppliers of programs to be carried over cable systems): "limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest." 47 U.S.C. § 533(f)(a)(1)(B). The FCC has duly promulgated regulations. See 47 C.F.R. § 76.503-04. Petitioners Time Warner and AT&T challenge the horizontal limit as in excess of statutory authority, as unconstitutional infringements of their freedom of speech, and as products of arbitrary and capricious decisionmaking which violate the Administrative Procedure Act. Time Warner similarly challenges the vertical limit. Together with AT&T, Time Warner also challenges as arbitrary and capricious the rules for determining what counts as an "attributable interest." Concluding that the FCC has not met its burden under the First Amendment and, in part, lacks statutory authority for its actions, we remand for further consideration of both limits. In addition we vacate specific portions of the attribution

rules as lacking rational justification.

Consumers Union also files a petition for review, which need not detain us long. It objects to the Commission's action to the extent that it continued a stay on enforcement of the horizontal limit. See *Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992*, 14 F.C.C.R. 19098, 19127-28 ¶ ¶ 71-73 (1999) ("Third Report"). The Commission issued the stay after a district court found the statute underlying that limit unconstitutional, see *Daniels Cablevision, Inc. v. United States*, 835 F. Supp. 1 (D.D.C. 1993), and provided that in the event of *Daniels*'s reversal the stay would end. See *Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 F.C.C.R. 8565, 8609 ¶ 109 (1993) ("Second Report"). We did reverse *Daniels* in *Time Warner Entertainment Co. v. United States*, 211 F.3d 1313 (D.C. Cir. 2000) ("*Time Warner I*"), so the stay ended automatically.[1] Thus the stay issue is moot unless the issue posed is capable of repetition yet evading review. Even if we assume that the issue evades review, its recurrence is not probable enough to qualify it as "capable of repetition." See *Spencer v. Kemna*, 523 U.S. 1, 17 (1998) (requiring "a reasonable expectation that the same complaining party [will] be subject to the same action again") (internal citations omitted). Although we find here that the regulations fail constitutional scrutiny, the specific condition that led to the stay – a pending challenge to the *statute*'s constitutionality – is highly unlikely to recur. We therefore find Consumers Union's claim moot and dismiss the petition.

* * *

The horizontal rule imposes a 30% limit on the number of

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[1]The cross-appeals of the government and the cable firms from the district court's decision in *Daniels* were originally consolidated with the cable firms' petitions for review of earlier iterations of the implementing regulations. See *Time Warner I*, 211 F.3d at 1315-16. After a date for oral argument was set, the FCC initiated a new rulemaking as part of its planned quinquennial review of the horizontal regulations. We therefore severed the *Daniels* appeals from the challenges to the regulations, holding the latter in abeyance until the completion of the new rulemaking. See *id.* The challenge to the new horizontal rules has supplanted that portion of the earlier challenges.

subscribers that may be served by a multiple cable system operator ("MSO"). See 47 C.F.R. § 76.503; *Third Report* 14 F.C.C.R. at 19119 ¶ 55. Both the numerator and denominator of this fraction include only current subscribers to multichannel video program distributor ("MVPD") services. See *id.* at 19107-10 ¶ ¶ 20-25. Subscribers include not only users of traditional cable services but also subscribers to non-cable MVPD services such as Direct Broadcast Satellite ("DBS"),[2] a rapidly growing segment of the MVPD market. See *id.* at 19110-12 ¶ ¶ 26-35. The Commission pointed out that under this provision the nominal 30% limit would allow a cable operator to serve 36.7% of the nation's cable subscribers if it served none by DBS. See *id.* at 19113 ¶ 37 & n.82.[3] In an express effort to encourage competition through new provision of cable, the Commission excluded from any MSO's numerator all new subscribers signed up by virtue of "overbuilding," the industry's term for cable laid in competition with a pre-existing cable operator. See *id.* at 19112-13 ¶ ¶ 34, 37. Further, subscribers to a service franchised after the rule's adoption (October 20, 1999) do not go into an MSO's numerator, even if not the result of an overbuild. See *id.* at 19112 ¶ 33. As a result, the rule's main bite is on firms obtaining subscribers through merger or acquisition.

The vertical limit is currently set at 40% of channel capacity, reserving 60% for programming by non-affiliated firms. See 47 C.F.R. § 76.504; *Second Report*, 8 F.C.C.R. at 8593- 94 ¶ 68; *Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition*

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[2]DBS "is a nationally distributed subscription video service that delivers programming via satellite to a small parabolic 'dish' antenna located at the viewer's home." *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Program ming*, Seventh Annual Report, CS Docket No. 00-132, FCC 01-01 (rel. Jan. 8, 2001) ¶ 71 (2000) ("Seventh Annual Report").

[3]30% of roughly 80 million MVPD subscribers would be about 24 million subscribers, which in turn would be 36.69% of roughly 66 million cable subscribers. Under the Commissions most recent subscriber estimates, this provision would allow an MSO to serve 37.4% of cable subscribers, or approximately 1.1 million more customers than when the *Third Report* was written. See *Seventh Annual Report* at ¶ ¶ 6-7.

Act of 1992, 10 F.C.C.R. 7364, 7368 ¶ 14 (1995) ("Reconsideration Order"). Channels assigned to broadcast stations, leased access, and for public, educational, or governmental uses are included in the calculation of channel capacity. See *id.* at 7371-73 ¶¶ 20- 27. Capacity over 75 channels is not subject to the limit, so a cable operator is never required to reserve more than 45 channels for others (.60 x 75 = 45). See *id.* at 7374-76 ¶¶ 31-35.

As cable operators, Time Warner and AT&T "exercise[ ] editorial discretion in selecting the programming [they] will make available to [their] subscribers," *Time Warner I*, 211 F.3d at 1316, and are "entitled to the protection of the speech and press provisions of the First Amendment," *Turner Broadcasting System, Inc. v. Federal Communications Commission*, 512 U.S. 622, 636 (1994) ("*Turner I*") (quoting *Leathers v. Medlock*, 499 U.S. 439, 444 (1991)). The horizontal limit interferes with petitioners' speech rights by restricting the number of viewers to whom they can speak. The vertical limit restricts their ability to exercise their editorial control over a portion of the content they transmit.

In *Time Warner I* we upheld the statutory provisions against a facial attack, after finding them subject to intermediate rather than, as the cable firms argued, strict scrutiny. *Time Warner I*, 211 F.3d at 1316-22. The regulations here present a related but independent set of questions. Constitutional authority to impose some limit is not authority to impose any limit imaginable.

In briefs written before the issuance of *Time Warner I*, petitioners argued here for strict scrutiny. At oral argument they withdrew from this position and said, euphemistically, that they were "happy to stand on intermediate scrutiny." Because of that concession and, in any event, not seeing any distinction between the statute and the regulations for level of-scrutiny purposes, we apply intermediate scrutiny. Under the formula set forth in *United States v. O'Brien*, 391 U.S. 367, 377 (1968), and reaffirmed by *Turner Broadcasting System, Inc. v. Federal Communications Commission*, 520 U.S. 180, 189 (1997) ("*Turner II*"), a governmental regulation subject to intermediate scrutiny will be upheld if it "advances important governmental interests unrelated to the suppression of free speech and does not burden substantially more

speech than necessary to further those interests." *Id.* (quoting *O'Brien*, 391 U.S. at 377).

The interests asserted in support of the horizontal and vertical limits are the same interrelated interests that we found sufficient to support the statutory scheme in *Time Warner I*: "the promotion of diversity in ideas and speech" and "the preservation of competition." *Time Warner I*, 211 F.2d at 1319; see also *Turner I*, 512 U.S. at 662-64 (concluding that both qualify as important governmental interests). After a review of the legislative history, we concluded that Congress had drawn "reasonable inferences, based upon substantial evidence, that increases in the concentration of cable operators threatened diversity and competition in the cable industry." *Time Warner I*, 211 F.3d at 1319-20. But the FCC must still justify the limits that it has chosen as not burdening substantially more speech than necessary. In addition, in "demonstrat[ing] that the recited harms are real, not merely conjectural," *Turner I*, 512 U.S. at 664, the FCC must show a record that validates the *regulations*, not just the abstract statutory authority.

* * *

The FCC asserts that a 30% horizontal limit satisfies its statutory obligation to ensure that no single "cable operator or group of cable operators can unfairly impede ... the flow of video programming from the video programmer to the consumer," 47 U.S.C. § 533(f)(2)(A), while adequately respecting the benefits of clustering[4] and the economies of scale that are thought to come with larger size. See *Third Report*, 14 F.C.C.R. at 19123-24 ¶ 61. It interpreted this statutory language as a directive to prohibit large MSO—either by the action of a single MSO or the coincidental or collusive actions of several MSO—from precluding the entry into the market of a new cable programmer. See *id.* at

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[4]"Clustering" refers to the strategy under which MSO concentrate their operations within a particular geographic region, giving up scattered holdings around the country. The benefits are thought to be in achieving economies of both scale and scope, allowing MSO to spread fixed investment costs over a larger customer base and to better compete with telephone companies owning local loops that are actual or potential substitutes. See *Seventh Report* ¶ ¶ 152-53.

19116 ¶ 43. In setting the limit at 30%, it assumed there was a serious risk of collusion. See *id.*, Part VI, at 19113-25 ¶¶ 36-65. But while collusion is a form of anti-competitive behavior that implicates an important government interest, the FCC has not presented the "substantial evidence" required by *Turner I* and *Turner II* that such collusion has in fact occurred or is likely to occur; so its assumptions are mere conjecture. See *Turner II*, 520 U.S. at 195 (citing *Turner I*, 512 U.S. at 666). The FCC alternatively relies on its supposed grant of authority to regulate the non-collusive actions of large MSOs. Congress may indeed, under certain readings of *Turner I* and *Turner II*, have the power to regulate the coincidental but independent actions of cable operators solely in the interest of diversity, but "[where an administrative interpretation of a statute invokes the outer limits of Congress' power, we expect a clear indication that Congress intended that result." *Solid Waste Agency v. United States Army Corps of Angriest*, __ U.S. __, 121 S. Ct. 675, 683 (2001). The 1992 Cable Act, as we shall see, instead expresses the contrary intention.

Part VI of the *Third Report* lays out the calculations that lead the FCC to the 30% limit. See *Third Report*, Part VI, 14 F.C.C.R. at 19113-25 ¶¶ 36-65. First the FCC determines that the average cable network needs to reach 15 million subscribers to be economically viable. See *id.* at 19114-16 ¶¶ 40-42. This is 18.56% of the roughly 80 million MVPD subscribers, and the FCC rounds it up to 20% of such subscribers. The FCC then divines that the average cable programmer will succeed in reaching only about 50% of the subscribers linked to cable companies that *agree* to carry its programming, because of channel capacity, "programming tastes of particular cable operators," or other factors. *Id.* at 19117-18 ¶ 49. The average programmer therefore requires an "open field" of 40% of the market to be viable (.20/.50 = .40). See *id.* at 19117-18 ¶¶ 46-50.

Finally, to support the 30% limit that it says is necessary to assure this minimum, the Commission reasons as follows: With a 30% limit, a programmer has an "open field" of 40% of the market even if the two largest cable companies deny carriage, acting "individually or collusively." *Id.* at 19119 ¶ 53. A 50% rule is inadequate because, if a

duopoly were to result, "[t]he probability of tacit collusion is higher with 2 competitors than 3 competitors." *Id.* at 19118-19 ¶ 51. Even if collusion were not to occur, *independent* rejections by two MSOs could doom a new programmer, thwarting congressional intent as the Commission saw it. See *id.* A 40% limit is insufficient for the same reason: "two MSOs, ... representing a total of 80% of the market, might decline to carry the new network" and leave only 20% "open," which by hypothesis is not enough (because of the 50% success rate). *Id.* at 19119 ¶ 52. Although the Commission doesn't spell out the intellectual process, it is necessarily defining the requisite "open field" as the residue of the market after a programmer is turned down either (1) by one cable company acting alone, or (2) by a set of companies acting either (a) collusively or (b) independently but nonetheless in some way that, because of the combined effect of their choices, threatens fulfillment of the statutory purposes. We address the FCC's authority to regulate each of these scenarios in turn.

The Commission is on solid ground in asserting authority to be sure that no single company could be in a position singlehandedly to deal a programmer a death blow. Statutory authority flows plainly from the instruction that the Commission's regulations "ensure that no cable operator or group of cable operators can unfairly impede, either because of *the size of any individual operator* or because of joint actions of operators of sufficient size, the flow of video programming from the video programmer to the consumer." 47 U.S.C. § 533(f)(2)(A) (emphasis added). Constitutional authority is equally plain. As the Supreme Court said in *Turner II*: "We have identified a corresponding 'governmental purpose of the highest order' in ensuring public access to 'a multiplicity of information sources.' " 520 U.S. at 190 (quoting *Turner I*, 512 U.S. at 663); see also *Time Warner Entertainment Co. v. Federal Communications Commission*, 93 F.3d 957, 969 (D.C. Cir. 1996). If this interest in diversity is to mean anything in this context, the government must be able to ensure that a programmer have at least two conduits through which it can reach the number of viewers needed for viability—independent of concerns over anticompetitive conduct.

Assuming the validity of the premises supporting the FCC's

conclusion that a 40% "open field" is necessary (a question that we need not answer here), the statute's express concern for the act of "any individual operator" would justify a horizontal limit of 60%. To reach the 30% limit, the FCC's action necessarily involves one or the other of two additional propositions: Either there is a material risk of collusive denial of carriage by two or more companies, or the statute authorizes the Commission to protect programmers against the risk of completely *independent* rejections by two or more companies leaving less than 40% of the MVPD audience potentially accessible. Neither proposition is sound.

First, we consider whether there is record support for inferring a non-conjectural risk of collusive rejection. Either Congress or the Commission could supply that record, and we take them in that order. We give deference to the predictive judgments of Congress, see *Turner II*, 520 U.S. at 195-96 (citing *Turner I*, 512 U.S. at 665), but Congress appears to have made no judgment regarding collusion. The statute plainly alludes to the *possibility* of collusion when it authorizes regulations to protect against "*joint* actions by a group of operators of sufficient size." 47 U.S.C. § 533(f)(2)(A) (emphasis added). But this phrase, while granting the Commission authority to take action in the event that it finds collusion extant or likely, is not itself a congressional finding of actual or probable collusion. Such findings have not been made. No reference to collusion appears in the Act's findings or policy, see 1992 Cable Act § 2, 106 Stat. at 1460-63, nor in the legislative history discussing the horizontal or vertical limits. See H.R. Rep. No. 102-628, at 40-43 (1992) ("House Report"); S. Rep. No. 102-92, at 24-29, 32-34, reprinted in 1991 U.S.C.C.A.N. 1133, at 1156-62, 1165-67 ("Senate Report"). It was thus appropriate for the FCC to describe Congress's reference to "joint" action as merely a "legislative *assumption*." *Third Report*, 14 F.C.C.R. at 19116 ¶ 43 (emphasis added).

The Commission's own findings amount to precious little. It says only:

> The legislative assumption [about joint action] is not unreasonable given an environment in which all the larger operators in the industry are vertically integrated so that all are both buyers

> and sellers of programming and have mutual incentives to reach carriage decisions beneficial to each other. Operators have incentives to agree to buy their programming from one another. Moreover, they have incentives to encourage one another to carry the same non-vertically integrated programming in order to share the costs of such programming.

Id. None of these assertions is supported in the record. The Commission never explains why the vertical integration of MSOs gives them "mutual incentive to reach carriage decisions beneficial to each other," what may be the firms' "incentives to buy ... from one another," or what the probabilities are that firms would engage in reciprocal buying (presumably to reduce each other's average programming costs). After all, the economy is filled with firms that, like MSOs, display partial upstream vertical integration. If that phenomenon implies the sort of collusion the Commission infers, one would expect the Commission to be able to point to examples. Yet it names none. Further, even if one accepts the proposition that an MSO could benefit from sharing the services of specific programmers, programming is not more attractive for this purpose merely because it originates with another MSO's affiliate rather than with an independent.

The only justification that the FCC offers in support of its collusion hypothesis is the economic commonplace that, all other things being equal, collusion is less likely when there are more firms. See *Third Report* 14 F.C.C.R. at 19118-19 ¶ 51. This observation will always be true, although marginally less so for each additional firm; but by itself it lends no insight into the question of what the appropriate horizontal limit is. *Turner I* demands that the FCC do more than "simply 'posit the existence of the disease sought to be cured.' " *Turner I*, 512 U.S. at 664 (quoting *Quincy Cable TV, Inc. v. Federal Communications Commission*, 768 F.2d 1434, 1455 (D.C. Cir. 1985). It requires that the FCC draw "reasonable inferences based on substantial evidence." *Turner I*, 512 U.S. at 666. Substantial evidence does not require a complete factual record—we must give appropriate deference to predictive judgments that necessarily involve the expertise and experience of the agency. See *Turner II* 520 U.S. at 196, citing *Federal Commu-*

nications Commission v. National Citizens Comm. For Broadcasting, 436 U.S. 775, 814 (1978). But the FCC has put forth no evidence at all that indicates the prospects for collusion.

That having been said, we do not foreclose the possibility that there are theories of anti-competitive behavior other than collusion that may be relevant to the horizontal limit and on which the FCC may be able to rely on remand. See 47 U.S.C. § 533(f)(1). Indeed, Congress considered, among other things, the ability of MSOs dominant in specific cable markets to extort equity from programmers or force exclusive contracts on them. See 1992 Cable Act § 2(a)(4)-(5), 106 Stat. at 1460-61; Senate Report at 3, 14, 23-29, 32-34, reprinted in 1991 U.S.C.C.A.N. at 1135, 1146-47, 1156-62, 1165-67; House Report at 40-43. A single MSO, acting alone rather than "jointly," might perhaps be able to do so while serving somewhat less than the 60% of the market (i.e., less than the fraction that would allow it unilaterally to lock out a new cable programmer) despite the existence of antitrust laws and specific behavioral prohibitions enacted as part of the 1992 Cable Act, see 47 U.S.C. § 536, and the risk might justify a prophylactic limit under the statute. See *Time Warner I*, 211 F.3d at 1322-23. So the absence of any showing of a serious risk of collusion does not *necessarily* preclude a finding of a sufficient governmental interest in preventing unfair competition. (We express no opinion on whether exploitation of a monopoly position in a specific cable market to extract rents that would otherwise flow to programmers alone gives rise to an "important governmental interest" justifying a burden on speech.) But the FCC made no attempt to justify its regulation on these grounds.

We pause here to address an aspect of petitioners' statutory challenge that is relevant to a showing of non-conjectural harm. Congress required that in setting the horizontal limit, the FCC "take particular account of the market structure ... including the nature and market power of the local franchise." 47 U.S.C. § 533(f)(2)(C). Petitioners assert that the Commission's failure to take adequate account of the competitive pressures brought by the availability and increasing success of DBS make the horizontal limit arbitrary and capricious. Although DBS accounts for only 15.4% of current MVPD households,

the annual increase in its total subscribership is almost three times that of cable (nearly three million additional subscribers over the period June 1999 to June 2000, as against one million for cable). See *Seventh Annual Report* ¶ ¶ 6-8. To the extent petitioners argue that the horizontal limit must fail because market share does not *equal* market power, they misconstrue the statutory command. The Commission is not required to design a limit that falls solely on firms possessing market power.[5] The provision is directed to the Commission's intellectual process, and requires it, in evaluating the harms posed by concentration and in setting the subscriber limit, to assess the determinants of market power in the cable industry and to draw a connection between market power and the limit set.

It follows naturally from our earlier discussion that we do not believe the Commission has satisfied this obligation. Having failed to identify a non-conjectural harm, the Commission could not possibly have addressed the connection between the harm and market power. But the assessment of a real risk of anti-competitive behavior—collusive or not—is itself dependent on an understanding of market power, and the Commission's statements in the *Third Report* seem to ignore the true relevance of competition. In changing the calculation of the horizontal limit to reflect subscribers instead of homes at which a service is available, for instance, the Commission wrote:

> [W]hether subscribership or homes passed data is used is largely a mechanical issue in terms of the market power issue.... As the market develops in terms of competition we believe ... that an operator's actual number of subscribers more uniformly and accurately reflects pow-er in the programming marketplace. *Third Report*, 14 F.C.C.R. at 19108 ¶ 22.

But normally a company's ability to exercise market power depends not only on its share of the market, but also on the elasticities

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[5]Contrast Congress's requirement that the FCC "*make* such rules and regulations reflect the dynamic nature of the communications marketplace." 47 U.S.C. § 533(f)(2)(E) (emphasis added).

of supply and demand, which in turn are determined by the *availability* of competition. See *AT&T Corp. v. Federal Communications Commission*, 236 F.3d 729, 736 (D.C. Cir. 2001). If an MVPD refuses to offer new programming, customers with access to an alternative MVPD may switch. The FCC shows no reason why this logic does not apply to the cable industry. Indeed, its most recent competition report suggests that it does. According to the Commission, "several very small and rural cable systems have used a variety of schemes to add digital channels, expand their program offerings, and take preemptive action against aggressive DBS marketing." *Seventh Annual Report* ¶ 67.

Given the substantial changes in the cable industry since publication of the *Third Report* in 1999 and our reversal on other grounds, there is little point in our reviewing the Commission's assessment of then-existing market power of cable MVPDs. But whatever conclusions are to be drawn from the new data, it seems clear that in revisiting the horizontal rules the Commission will have to take account of the impact of DBS on that market power. Already when the *Third Report* was written, DBS could be considered to "pass every home in the country." *Third Report*, 14 F.C.C.R. at 19107-08 ¶ 20. The technological and regulatory changes since then appear only to strengthen petitioners' contention. See *Seventh Annual Report* ¶ ¶ 60-82, 140.

With the risk of collusion inadequately substantiated to support the 30% limit and no attempt to find other anticompetitive behavior, there remains the Commission's alternative ground—that programming choices made "unilaterally" by multiple cable companies, *Third Report*, 14 F.C.C.R. at 19118-19 ¶ 51; see also *id.* at 19119 ¶ 53 ("individually"), might reduce a programmer's "open field" below the 40% benchmark. The only support the Commission offered for regulation based on this possibility was the idea that every additional chance for a programmer to secure access would enhance diversity:

> [T]he 30% limit serves the salutary purpose of ensuring that there will be at least 4 MSOs in the marketplace. The rule thus maximizes the potential number of MSOs that will purchase programming. With more MSOs making purchasing decisions, this increases the likelihood that the MSOs will make different

> programming choices and a greater variety of media voices will therefore be available to the public.

Id. ¶ 54. Petitioners challenge the FCC's authority to regulate for this purpose on both constitutional and statutory grounds.

We have some concern how far such a theory may be pressed against First Amendment norms. Everything else being equal, each additional "voice" may be said to enhance diversity. And in this special context, every additional splintering of the cable industry increases the number of *combinations* of companies whose acceptance would in the aggregate lay the foundations for a programmer's viability. But at some point, surely, the marginal value of such an increment in "diversity" would not qualify as an "important" governmental interest. Is moving from 100 possible combinations to 101 "important"? It is not clear to us how a court could determine the point where gaining such an increment is no longer important. And it would be odd to discover that although a newspaper that is the only general daily in a metropolitan area cannot be subjected to a right of reply, see *Miami Herald Publishing Co. v. Tornillo*, 418 U.S. 241 (1974), it could in the name of diversity be forced to self-divide. Certainly the Supreme Court has not gone so far.

We need not face that issue, however, because we conclude that Congress has not given the Commission authority to impose, solely on the basis of the "diversity" precept, a limit that does more than guarantee a programmer two possible outlets (each of them a market adequate for viability). We analyze the agency action under the familiar framework of *Chevron USA, Inc. v. National Resources Defense Council, Inc.*, 467 U.S. 837 (1984). If we find (using traditional tools of statutory interpretation) that Congress has resolved the question, that is the end of the matter. *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 132 (2000); *National Resources Defense Council, Inc. v. Browner*, 57 F.3d 1122, 1125 (D.C. Cir. 1995). We must place the statutory language in context and "interpret the statute 'as a symmetrical and coherent regulatory scheme.' " *Brown & Williamson*, 529 U.S. at 133.

We begin with the statutory language. The relevant section requires the FCC

> to ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video program-ming from the video programmer to the consumer.

47 U.S.C. § 533(f)(2)(A).

The language addresses only "unfair[ ]" impediments to the flow of programming. The word "unfair" is of course extremely vague. Certainly, the action of several firms that is "joint," in the sense of collusive, may often entail unfairness of a conventional sort. The statute goes further, plainly treating exercise of editorial discretion by a single cable operator as "unfair" simply because that operator is the only game in town. (And *Time Warner I* authoritatively determines that the government is constitutionally entitled to impose limits solely on that ground.) But we cannot see how the word unfair could plausibly apply to the legitimate, independent editorial choices of multiple MSOs. A broad interpretation is plausible *only* for actions that impinge at least to some degree on the interest in competition that lay at the heart of Congress's concern.[6] The Commission's reading of the clause effectively deletes the word "joint" and opens the door to illimitable restrictions in the name of diversity.

Looking at the statute as a whole does little to support the FCC's position. The "interrelated interests" of promoting diversity and fair competition run throughout the 1992 Cable Act's various provi-

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[6]The Commission's economic theory – that cable operators have an incentive to contract with the same programmers in order to lower the programmers' average costs (see discussion in the collusion context, *supra* p. 1152) – would seem to apply regardless of any horizontal limit. Putting various special cases aside, *any* profit-maximizing firm will have an incentive to lower its costs. In a market where a cable operator is a monopolist, the resulting benefit to the firm would be classified as monopoly rents. In a market where an operator is in competition, it can be expected to pass the benefits on to its customers. But the FCC has not shown why such pursuit of lower costs, by the monopolist or the competitive firm, is by itself "unfair," and the statute allows for regulation only if unfairness can be shown.

sions. *Turner II*, 520 U.S. at 189.[7] But despite the duality of interests at work in this section, see *Time Warner I*, 211 F.3d at 1319, it is clear from the structure of the statute that Congress's *primary* concern in authorizing ownership limits is "fair" competition. The statute specifies, after all, that *these* regulations are to be promulgated "[i]n order to enhance effective competition." 47 U.S.C. § 533 (f)(1). In only two of the other sections of the 1992 Cable Act does Congress specify a dominant purpose.[8] This statement of purpose supports a reading that sharply confines the authority to regulate solely in the interest of diversity.

The FCC points to the statutory findings that the "cable industry has become highly concentrated" and that "the potential effects of such concentration are barriers to entry for new programmers and a reduction in the number of media voices available to consumers." *Third Report*, 14 F.C.C.R. at 19118-19 ¶ 51, 1992 Cable Act § 2(a)(4), 106 Stat. at 1460. But reference to a congressional finding cannot overcome the clear language and purpose of the actual provision. The quoted finding stands as little more than support for the proposition that Congress was concerned with the possibilities for market failure and the possible impact on new programmers. The legislative history also offers little. Again, the fact that Congress's interest in anti-competitive behavior may have been animated by an interest in preserving diversity doesn't give the FCC carte blanche to cobble cable operators in the

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[7]The 1992 Cable Act is a wide-ranging statute that includes, besides the ownership limits, must-carry and leased-access requirements, rate regulation, behavioral prohibitions, and privacy protections. See 1992 Cable Act, 106 Stat. 1460.

[8]The leased access provision was amended to add the words "to promote competition in the delivery of diverse sources of video programming" to the section's previously stated purpose of assuring "that the widest possible diversity of information sources are made available." 1992 Cable Act § 9(a), 106 Stat. at 1484; 47 U.S.C. § 532(a). The various behavioral rules designed to prevent cable operators from abusing their market power were passed for the stated purpose of promoting "the public interest, convenience, and necessity by increasing competition and diversity in the multichannel video programming market." 1992 Cable Act § 19, 106 Stat. at 1494; 47 U.S.C. § 547.

name of the latter value alone. After all, Congress also sought to "ensure that cable operators continue to expand, where economically justified, their capacity," 1992 Cable Act § 2(b)(3), 106 Stat. at 1463, and it specifically directed the FCC, in setting the ownership limit, to take into account the "efficiencies and other benefits that might be gained through increased ownership or control." 47 U.S.C. § 533(f)(2)(D).

On the record before us, we conclude that the 30% horizontal limit is in excess of statutory authority. While a 60% limit might be appropriate as necessary to ensure that programmers had an adequate "open field" even in the face of rejection by the largest company, the present record supports no more. In addition, the statute allows the Commission to act prophylactically against the risk of "unfair" conduct by cable operators that might unduly impede the flow of programming, either by the "joint" actions of two or more companies or the independent action of a single company of sufficient size. But the Commission has pointed to nothing in the record supporting a non-conjectural risk of anticompetitive behavior, either by collusion or other means. Accordingly, we reverse and remand with respect to the 30% rule.

* * *

The FCC presents its 40% vertical limit as advancing the same interests invoked in support of its statutory authority to adopt the rule: diversity in programming and fair competition. As with the horizontal rules the FCC must defend the rules themselves under intermediate scrutiny and justify its chosen limit as not burdening substantially more speech than necessary. Far from satisfying this test, the FCC seems to have plucked the 40% limit out of thin air.

The FCC relies almost exclusively on the congressional findings that vertical integration in the cable industry could "make it difficult for non-cable affiliated ... programmers to secure carriage on vertically integrated cable systems" and that "vertically integrated program suppliers have the incentive and the ability to favor their affiliated cable operators ... and program distributors." *Second Report*, 8 F.C.C.R. at 8583 ¶ 41 (citing 1992 Cable Act § 2(a)(5), 106 Stat. at 1460). Regulatory limits in response to these consequences would "increase the

diversity of voices available to the public." *Second Report*, 8 F.C.C.R. at 8583-84 ¶ 42 (citing Senate Report at 80, reprinted in 1991 U.S.C.C.A.N. at 1213). In *Time Warner I* we thought these findings strong enough to overcome the First Amendment challenge to the relevant provision of the 1992 Cable Act. In doing so, we held that such a prophylactic rule was not "rendered unnecessary merely because preexisting statutes [such as the antitrust laws and the antidiscrimination provisions of the 1992 Cable Act] impose behavioral norms." *Time Warner I*, 211 F.3d at 1322-23. Beyond that we did not assess the appropriateness of the burden on speech. We upheld no specific vertical limit—none was before us.

We recognize that in drawing a numerical line an agency will ultimately indulge in some inescapable residue of arbitrariness; even if 40% is a highly justifiable pick, no one could expect the Commission to show why it was materially better than 39% or 41%. See *Missouri Public Service Comm'n v. FERC*, 215 F.3d 1, 5 (D.C. Cir. 2000). But to pass even the arbitrary and capricious standard, the agency must at least reveal " 'a rational connection between the facts found and the choice made.' " *Dickson v. Secretary of Defense*, 68 F.3d 1396, 1404-05 (D.C. Cir. 1995) (quoting *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). Here the FCC must also meet First Amendment intermediate scrutiny. Yet it appears to provide nothing but the conclusion that "we believe that a 40% limit is appropriate to balance the goals." See *Second Report*, 8 F.C.C.R. at 8593-95 ¶ 68. What are the conditions that make 50% too high and 30% too low? How great is the risk presented by current market conditions? These questions are left unanswered by the Commission's discussion.

The FCC argued before us that no MSO has yet complained that the 40% vertical limit has required it to alter programming. This is no answer at all, as it says nothing about plans that the rule may have scuttled. Petitioners responded that their subsidiaries frequently must juggle their channel lineups to stay within the cap. Furthermore, it appears uncontested that AT&T's merger with MediaOne brings the vertical limits into play. See *In the Matter of Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from*

MediaOne Group, Inc. to AT&T Corporation, 15 F.C.C.R. 9816 (2000).

In fairness, the FCC does make an attempt to review some relevant conditions. See *Second Report*, 8 F.C.C.R. at 8583-85 ¶ ¶ 41-45. The FCC cites the House Report's conclusion that "some" vertically integrated MSOs favor their affiliates and "may" discriminate against others. *Id.* at 8583-84 ¶ 42 (citing House Report at 43). But it also notes a report that none of the top five MSOs "showed a pattern" of favoring their affiliates. *Id.* at 8584 ¶ 43. Indeed, the FCC concludes that "vertical relationships had increased both the quality and quantity of cable programming services." *Id.* ¶ 44. But still it settled on a limit of 40%. There is no effort to link the numerical limits to the benefits and detriments depicted. Further, given the pursuit of diversity, one might expect some inquiry into whether innovative independent originators of programming find greater success selling to affiliated or to unaffiliated programming firms, but there is none.

Quite apart from the numerical limit vel non, petitioners attack the Commission's refusal to exclude from the vertical limit cable operators that are subject to effective competition. The FCC had proposed exempting cable operators who met the definition of effective competition provided by § 623 of the Communications Act of 1934. See *Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 F.C.C.R. 6828, 6862 ¶ 231 (1993) ("First Report"); see also 47 U.S.C. § 543(*l*)(1) (defining the categories of cable operators that are not subject to rate regulation under that section).[9] Of course our decision in *Time Warner I* acknowledged the

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[9]The term "effective competition" means that—

(A) fewer than 30 percent of the households in the franchise area subscribe to the cable system;(B) the franchise area is—

(i) served by at least two unaffiliated multichannel video programming distributors each of which offers comparable video programming to at least 50 percent of the households in the franchise area; and

(ii) the number of households subscribing to programming services offered by multichannel video programming distributors other than the largest multichannel video programming distributor exceeds 15 percent of the households in the franchise area; or

existence of incentives to use affiliated programming. 211 F.3d at 1322. For example, even where an unaffiliated supplier offered a better cost quality trade-off, a company might be reluctant to ditch or curtail an inefficient in-house operation because of the impact on firm executives or other employees, or the resulting spotlight on management's earlier judgment. But petitioners argue, quite plausibly, that exposure to competition will have an impact on a cable company's *ability* to indulge in favoritism for in-house productions. After all, while reliance on inhouse suppliers offering an inferior price-quality trade-off will reduce a monopolist's profits, it may threaten a competitive firm's very survival. This analysis is not foreign to the Commission, which endorsed it when proposing the exemption:

> We believe that this proposal is appropriate since effective competition will preclude cable operators from exercising the market power which originally justified channel occupancy limits. Where systems face effective competition, their incentive to favor an affiliated programmer will be replaced by the incentive to provide programming that is most valued by subscribers. *First Report*, 8 F.C.C.R. at 6862 ¶ 231.

The FCC makes two arguments to justify its refusal to exempt MVPDs that are subject to effective competition. First, it says that the definition of competition provided by 47 U.S.C. § 543 was "not adopted for this specific purpose" but rather for relief from rate regulation. See *Reconsideration Order* 10 F.C.C.R. at 7379 ¶ 47. Indeed, we have recog-

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(C) a multichannel video programming distributor operated by the franchising authority for that franchise area offers video programming to at least 50 percent of the households in that franchise area; or

(D) a local exchange carrier or its affiliate (or any multichannel video programming distributor using the facilities of such carrier or its affiliate) offers video programming services ... in the franchise area of an unaffiliated cable operator which is providing cable service in that franchise area, but only if the video programming services so offered in that area are comparable to the video programming services provided by the unaffiliated cable operator in that area.

47 U.S.C. § 543(*l*)(1).

nized that one of the ways in which the statutory standard is met may be surprisingly defective as a mark of real competition. See *Time Warner Entertainment Co., L.P. v. Federal Communications Commission*, 56 F.3d 151, 166 (D.C. Cir. 1995) (MVPDs satisfying subsection (A) of 47 U.S.C. § 543(*l*)(1) (low penetration) may do so more as a result of geography than competition). But the Commission is free to carve out subsections that are truly pertinent to competition, as it had proposed. See *First Report*, 8 F.C.C.R. at 8662-63 ¶ 232; *Second Report*, 8 F.C.C.R. at 8602 ¶ 85.

Of course competition that is adequate to justify dispensing with rate regulation could still leave an undue likelihood of improper favoritism for affiliated programmers. But the possible failure of readily available criteria does not itself justify the use of so blunt a blade. Congress expressly directed the Commission to take "*particular* account of the market structure..., including the nature and market power of the local franchise." 47 U.S.C. § 533(f)(2)(C) (emphasis added). Because competition raises the stakes for a firm that sacrifices the optimal price-quality trade-off in its acquisition of programming, the issue seems to trigger the legislative directive. Yet the Commission seems to ignore its own conclusions about cable companies' incentives and constraints, and the dynamics of the programming industry. See *First Report*, 8 F.C.C.R. at 6862 ¶ 231. If the criteria of § 543(*l*)(1) are unsuitable, the Commission can consider concepts of effective competition that it finds more apt for these purposes.

Second, the FCC comments that if a competing MVPD favored *its* own affiliated programmers, the presence of competition would have no tendency to create room for independent programmers. See *Reconsideration Order* 10 F.C.C.R at 7379 ¶ 47. But this theory seems contradicted by the Commission's own observation, mentioned earlier, that no vertically integrated MPVD has complained of reaching the 40% limit. Vertically integrated MVPDs evidently use loads of independent programming. Further, although cable operators continue to expand their interests in programmers, "[t]he *proportion* of vertically integrated channels ... continue[d] to decline" for each of the last two years. *Sixth Annual Report*, 15 F.C.C.R. at 1058-59 ¶ 181, *Seventh Annual*

Report ¶ 173 (emphasis added). Even if competing MSOs filled all of their channels with affiliates' products (as unlikely as that seems), the Commission nowhere explains why, in the pursuit of diversity, the independence of competing vertically integrated MVPDs is inferior to the independence of unaffiliated programmers. In any event, the Commission's point here does not respond to the intuition that competition spurs a firm's search for the best price-quality trade-off.

In its brief the Commission adds the argument that truly effective competition under § 543(*l*)(1) existed only for a tiny fraction of cable systems. Indeed, it said in its *Sixth Annual Report* that of the nation's 33,000 cable community units, only 157 satisfy the definition through being in a market offering more than one wireline MVPD. *Sixth Annual Report*, 15 F.C.C.R. at 1045-46 ¶ 142. (In the *Seventh Annual Report* we learn that now 330, or 1% of the total, meet the competition standard through exposure to another MVPD; in this report the qualifier "wireline" is absent. See *Seventh Annual Report* ¶ 138.) But in determining whether or not the regulations burden substantially more speech than necessary, it is a weak move to point to the paucity of MVPDs facing competition if, as seems the case, it is easy to exempt them from the limit.

We find that the FCC has failed to justify its vertical limit as not burdening substantially more speech than necessary. Accordingly, we reverse and remand to the FCC for further consideration.

* * *

We turn, finally, to several aspects of the rules for attributing ownership for purposes of the horizontal and vertical limits, recently revised by the FCC and challenged by petitioners. See *Implementation of the Cable Television Consumer Protection and Competition Act of 1992*, 14 F.C.C.R. 19014 (1999) ("*Attribution Order*"). Petitioners suggest that these rules affect their ability to "speak" to subscribers because of their connection to the horizontal and vertical limits. But petitioners' speech rights are implicated only where their interest allows them to exercise editorial control, in which case attribution would be proper and it is the horizontal or vertical limit that constrains speech. The only effect of the attribution rules where no control is exercised is to limit the

extent of petitioners' investments in a particular class of companies. We therefore review the agency actions under the APA standards, to determine whether they are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." See 5 U.S.C. § 706(2)(A).

The FCC adopted as its starting point the pre-existing rules for attributing ownership of broadcast television stations, finding that the purposes of the rules are the same. See *Attribution Order*, 14 F.C.C.R. at 19030 ¶ 35; *Second Report* 8 F.C.C.R. at 8577-79, 8593-96 ¶ ¶ 30-35, 56-63. Under that standard, attribution is triggered by ownership of 5% of the voting shares of a company, with various exceptions. See *Attribution of Ownership Interests*, 97 FCC 2d 997 (1984). Because the decisions in the *Attribution Order* tracked, to a large degree, similar decisions related to the broadcast attribution rules, the FCC incorporated by reference much of the reasoning from the broadcast orders. See *Attribution Order*, 14 F.C.C.R. at 19015-16 ¶ 1.

Petitioners challenge the sufficiency and relevance of the Commission's evidence in support of the 5% attribution rule and its failure to adopt an alternative proposed by cable industry interests. They begin by asserting that the FCC improperly relied on two studies that were mentioned neither in the FCC's notice nor in any party's submission. See *Notice of Proposed Rulemaking*, 13 F.C.C.R. 12990 (1998). Although it is true that an agency cannot rest a rule on data " 'that, [in] critical degree, is known only to the agency,' " *Community Nutrition Institute v. Block*, 749 F.2d 50, 57 (D.C. Cir. 1984) (quoting *Portland Cement Ass'n v. Ruckelshaus*, 486 F.2d 375, 393 (D.C. Cir. 1973); see also *International Union, UAW v. OSHA*, 938 F.2d 1310, 1324-35 (D.C. Cir. 1991) (approving reliance on documents not exposed to comment if not "vital" to agency's support for rule), obviously not every cited document is "critical."

Here, although petitioners assert that the studies were the sole evidence cited by the FCC, the Commission also relied on a survey, used to support the 1984 broadcast attribution rules, showing that in widely held corporations, an owner of 5% or more would ordinarily be one of the two or three largest shareholders. See *Attribution Order*, 14 F.C.C.R. at 19034 ¶ 46; *Block*, 749 F.2d at 58 (1984) (new information

"expanded on and confirmed information"). The earlier rulemaking had inferred that with such ownership a holder of 5% or more would be able "to potentially affect the outcome of elective or discretionary decisions and to command the attention of management." *Attribution of Ownership Interests*, 97 FCC 2d at 1005-06 ¶ 14. This hardly seems implausible. Presumably an owner of 5% or more typically has enough of an interest to justify the burden of informing himself about the company's activities and trying to influence (or supplant) management, a fact that management would bear in mind in deciding to whose exhortations it should pay attention. Petitioners have not pointed to any evidence suggesting that the FCC's survey is no longer accurate, or that the conclusion they draw from it has been undermined.

Furthermore, in attacking the relevance of the new studies, the petitioners fail to acknowledge that the FCC sought a rule that would capture "*influence* or control," not just control. *Attribution Order*, 14 F.C.C.R. at 19015-16 ¶ 1 (emphasis added). The Commission specifically noted that a "firm does not need actual operational control over ... a company in order to exert influence." *Id.* at 19030-31 ¶ 36. This distinction also tends to rebut petitioners' critique of the Commission's reliance on the Securities and Exchange Commission's requirement that investors report to the SEC when their holdings exceed 5% of any class of a firm's shares. See 15 U.S.C. § 78m(d)(1). The FCC noted that the purpose of the SEC's requirement was to alert investors to *potential* changes in control, and reasoned that this was similar to its own purpose in the attribution rules, encompassing not merely control but influence. See *Attribution Order*, 14 F.C.C.R. at 19035 ¶ 49 (citing *Securities and Exchange Comm'n v. Savoy Indus., Inc.*, 587 F.2d 1149 (D.C. Cir. 1978)).

Finally, petitioners contend that it was arbitrary for the FCC to reject a "control certification" approach, such as it adopted for partnerships, under which a partner can avoid attribution if (but only if) it certifies to the absence of certain relationships that might betoken control. In this argument, petitioners make a classic apples-and-oranges mix, since the bases that they proposed for self-certification, see *Attribution Order* at 19024 ¶ 22, are quite different

from those adopted by the Commission for partnerships, see *id.* at 19038 ¶ 57 n.163. Even if corporations and partnerships were virtually identical, the Commission would hardly be guilty of self-contradiction if it rejected certification scheme A for corporations and accepted certification scheme B for partnerships. In any event, for corporations the Commission rejected a case-by-case approach on conventional grounds, observing that a bright-line rule was to be preferred because it "reduces regulatory costs, provides regulatory certainty, and permits planning of financial transactions." *Id.* at 19035 ¶ 48; see also *id.* at 19031 ¶ 38. Given an agency's very broad discretion whether to proceed by way of adjudication or rulemaking, see *N.L.R.B. v. Bell Aerospace Co.*, 416 U.S. 267, 294 (1974), and the reasonableness of the 5% criterion, we doubt there was need to explain further. The Commission did, however, observe that the certification proposals offered did "not take into account the variety of ways that an investor may exert influence or control over a company." *Id.* at 19030-31 ¶ 36. And it implicitly distinguished its treatment of partnerships when it said that a limited partner's influence may not be proportional to equity interest "because the extent of its power may be modified by contract." *Id.* at 19039 ¶ 61. Indeed, the Commission's certification rules for partnerships require voting restrictions that would not normally, and perhaps could not, be paralleled in the corporate world (such as abnegation of any power to remove the general partner except under extremely limited circumstances, see *id.* at 19038 ¶ 57 n.163). We find the Commission's discussion adequate.

We also uphold the FCC's adoption of an "equity-and-debt" rule to capture "nonattributable investments that could carry the potential for influence." *Id.* at 19047 ¶ 83. The rule triggers attribution "to an investor that holds an interest that exceeds 33% of the total asset value (equity plus debt) of the applicable entity." *Id.* at 19046-47 ¶ 82.[10]

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[10]The Commission often writes as if investors owned the assets of the companies in which they hold stock or bonds. See, e.g., *Attribution Order*, 14 F.C.C.R. at 19047-48 ¶ 84 n.230. No issue is made here of how its calculations are to be made, e.g., percentage of book value, percentage of market capitalization, or some other method, although

Petitioners attack the sufficiency of evidence to support both the rule itself and the selection of 33% as limit. They observe in particular that the Commission's own claims seem to depend on *combinations* of debt and equity *with* contractual rights. See, e.g., *id.* at 19047 ¶ 83. But the Commission explicitly relied on an earlier rulemaking, see, e.g., *id.* at 19047 ¶ 83, citing *Review of the Commission's Regulations Governing Attribution of Broadcast and Cable/MDS Interests*, 14 F.C.C.R. 12559 (1999) ("Broadcast Attribution Order"), which in turn relied on academic literature, see *id.* at 12589 ¶ 62 nn.132, 134. Petitioners offer no critique of that literature's relevance, and it is not our role to launch one on our own. So we must accept the Commission's basic finding.

Although petitioners independently attack the Commission's selection of 33% as the debt-and-equity limit, we are constrained in our review by the sketchy character of their attack on the basic theory. The Commission's choice of 33% certainly has modest support. It recited the numbers offered by various parties, which ranged from 10% to 50%, in some cases with variations dependent on the presence of special contract provisions. *Attribution Order*, 14 F.C.C.R. at 19048-49 ¶¶ 85-86. Obviously 33% is not far off the median, but, as the Commission says nothing to evaluate the numbers recited, that tells us little.

The Commission also cited its own past decisions, saying that it had used the same percentage for the parallel rule in its broadcast cross-interest policy, and that there it "does not appear to have had a disruptive effect," *id.* at 19048-49 ¶ 86, though without indicating what (if any) assessment it had made. And it referred to two prior adjudications. *Id.* (citing *Cleveland Television Corp.*, 91 FCC 2d 1129 (Rev. Bd. 1982), *aff'd, Cleveland Television Corp. v. Federal Communications Commission*, 732 F.2d 962 (D.C. Cir. 1984), and *Roy M. Speer*, 11 F.C.C.R. 18393 (1996)). In *Cleveland Television* it had simply held that a one-third preferred stock interest conferred " '*in*sufficient incidents of contingent

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the Commission has attempted "clarification" in the broadcast context by allowing applicants to choose their valuation method. See *Review of the Commission's Regulations Governing Attribution of Broadcast and Cable/MDS Interest*, MM Docket No. 94-150, FCC 00-438 (rel. Jan. 19, 2001)¶¶6-28 (2001) ("Attribution Clarification Order").

control' " under various policies, *Attribution Order*, 14 F.C.C.R. at 19048-49 ¶ 86 (emphasis added). In *Roy M. Spear*, it relied on *Cleveland Television* to impose a 33% ownership on a creditor's purchase option, but deferred establishment of any general rule. See 11 F.C.C.R. 18393 ¶ 126 n.26. These prior adjudications provide thin affirmative support for the choice of 33%, though they at least suggest that the Commission has not indulged in self-contradiction. But given the absence of a real probe of the Commission's underlying reasoning for having the restriction at all, the inevitable difficulty in picking such a number, and the deference due the Commission, we cannot find the choice of 33% arbitrary. See *Cassell v. Federal Communications Commission*, 154 F.3d 478, 485 (D.C. Cir. 1998).

Petitioners also challenge the Commission's elimination of an exemption that prevailed in the broadcast attribution rules at the time the cable attribution rules were promulgated. In the broadcast context, an otherwise covered minority shareholder in a company with a single majority shareholder was exempted, on the principle that in such a case the minority shareholder would ordinarily not be able to direct the activities of the company.[11] See *Attribution of Ownership Interests*, 97 FCC 2d at 1008-09 ¶ 21; *Attribution Order*, 14 F.C.C.R. at 19044-46 ¶ ¶ 74-81. There were contentions in the *Broadcast Attribution Order* proceeding that the majority shareholder exemption was being used evasively. See 14 F.C.C.R. at 12574-75 ¶ 29. The Commission neither rejected nor accepted these claims, but retained the exemption. See *id.* at ¶ 36. In dispatching the exemption here, the Commission cited only its concern that a minority shareholder *might* be able to exercise influence even in these circumstances, the "lack of a record ... that the exemption should be retained," and the fact that no one claimed to be using the exemption. *Attribution Order*, 14 F.C.C.R. at 19046 ¶ 81.

The Commission argues here that petitioners lack standing because they have not shown that they are using the exemption.

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[11]The FCC has since eliminated the single majority owner exemption in the broadcast rules to bring it into conformity with the cable rules. See *Attribution Clarification Order* at ¶¶ 41-44.

Again, the FCC disregards the impact the rule can have on investment plans. Petitioners say that they are continually reviewing investment opportunities and that they are constrained by the absence of the single majority exemption. See *supra* p. 20. This is an actual "injury in fact" that is "fairly traceable" to the administrative action. See *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 561 (1992); see also *Committee for Effective Cellular Rules v. Federal Communications Commission*, 53 F.3d 1309, 1315-16 (D.C. Cir. 1995). And of course the absence of current use is no reason to delete an exemption. Removal of the exemption is a tightening of the regulatory screws, if perhaps a minor one. It requires some affirmative justification, cf. *State Farm*, 463 U.S. at 41-42 (requiring justification for removal of a restriction), yet the Commission effectively offers none. Its "concern" about the possibility of influence would be a basis, if supported by some finding grounded in experience or reason, but the Commission made no finding at all. Accordingly, deletion of the exemption cannot stand.

Finally, petitioners object to one of the seven criteria that a cable operator must satisfy in order to be exempt from attribution of limited partnership. The general rule is that *any* partnership interest, no matter how small, leads to attribution, *Attribution Order*, 14 F.C.C.R. at 19039-40 ¶ 61, but a limited partner can secure exemption if it certifies compliance with certain criteria intended to ensure that the partner "will not be materially involved in the media management and operations of the partnership." *Id.* The Commission interprets one of these criteria to bar exemption when a limited partner that is a vertically integrated MSO also sells programming to the partnership. See *id.* at 19055 ¶ 106. This criterion applies even though the limited partner, to achieve exemption, must have certified that it does not "communicate with the licensee or general partners on matters pertaining to the day-to-day operations of its video programming business." *Id.* at 19040-41 ¶ 64.

We agree with petitioners that the no-sale criterion bears no rational relation to the goal, as the Commission has drawn no connection between the sale of programming and the ability of a limited partner to control programming choices. Of course a programmer might secure contract terms giving it some control over a partnership's

programming choices, but, given the independent criterion barring even communications on the video-programming business, see *Attribution Order*, 14 F.C.C.R. at 19040-41 ¶ 64, exercise of that power would seem to be barred. Even if it weren't, the bargaining opportunity would depend on the desirability of the partner's programming, *not* on its status as a partner. The FCC does not even offer a hypothetical to the contrary.

* * *

To summarize, we reverse and remand the horizontal and vertical limits, including the refusal to exempt cable operators subject to effective competition from the vertical limits, for further proceedings. We also reverse and remand the elimination of the majority shareholder exception and the prohibition on sale of programming by an insulated limited partner. We uphold the basic 5% attribution rule and the creation of a 33% equity-and-debt rule.

So ordered

App. 30

United States Court of Appeals
For the District of Columbia Circuit

No. 94-1035 September Term, 2000

Filed On:
UNITED STATES COURT OF APPEALS
FOR DISTRICT OF COLUMBIA CIRCUIT
FILED
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Time Warner Entertainment Co., L.P.,
Petitioner

v.

Federal Communications Commission and United States of America,
Respondents

BellSouth Corporation, et al.,
Intervenors

Consolidated with 95-1337, 99-1503, 99-1504, 99-1522, 99-1541, 99-1542, 00-1086,

BEFORE: Edwards, Chief Judge; Williams, Ginsburg, Sentelle, Henderson, Randolph, Rogers, Tatel and Garland, Circuit Judges

ORDER

Upon consideration of intervenors' petition for rehearing en banc, and the absence of a request by any member of the court for a vote, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT
Mark J. Langer, Clerk

BY: s/Robert A. Bonner
Robert A. Bonner
Deputy Clerk

Circuit Judges Henderson and Garland did not participate in this matter.

App. 32
FCC 92-542

IN THE MATTER OF IMPLEMENTATION OF SECTIONS 11 AND 13 OF THE CABLE TELEVISION CONSUMER PROTECTION AND COMPETITION ACT OF 1992 HORIZONTAL AND VERTICAL OWNERSHIP LIMITS, CROSS-OWNERSHIP LIMITATIONS AND ANTI-TRAFFICKING PROVISIONS

MM Docket No. 92-264
Adopted: December 10, 1992; Released: December 28, 1992

NOTICE OF PROPOSED RULE MAKING AND NOTICE OF INQUIRY

Comment Date: February 9, 1993
Reply Comment Date: March 3, 1993
By the Commission:

I. INTRODUCTION

1. On October 5, 1992, Congress enacted the Cable Television Consumer Protection and Competition Act of 1992[1] By this Notice of Proposed Rule Making and Notice of Inquiry ("Notice") we seek comment on the interpretation and implementation of the cross-ownership and anti-trafficking provisions of the 1992 Cable Act. We also seek comment on the adoption of limits on horizontal concentration and vertical integration in the cable industry.

II. BACKGROUND

2. Section 13 of the 1992 Cable Act adds a new Section 617 to the Communications Act of 1934, as *amended*[2] *which establishes a three year*

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[1] Cable Television Consumer Protection and Competition Act of 1992, Pub.L. No. 102-385, 106 Stat. 1460 ("Cable Act of 1992" or "1992 Cable Act").

[2] The Communications Act of 1934, as amended, 47 U.S.C. § 151 et seq. ("Communications Act of 1934").

holding requirement for cable systems. This cable anti-trafficking rule, with certain exceptions, prohibits the sale or transfer of ownership in a cable system within three years following the acquisition or initial construction of such system. Section 11 of the Cable Act of 1992 establishes several restrictions on the ownership and sale of cable systems. First it modifies Section 613(a) of the Communications Act of 1934, as amended, to prohibit the common ownership of a cable system and a multichannel multipoint distribution service ("MMDS") or a cable system and a satellite master antenna television service ("SMATV"), apart from the franchised cable service, within a franchise area. Section 11 of the new Act also amends Section 613 of the Communications Act of 1934 by adding a new subsection (f)(1), which requires the Commission to conduct a proceeding: (1) to prescribe reasonable limits on the number of cable subscribers "a person can reach through cable systems owned by such person ("subscriber limits"); (2) to prescribe reasonable limits on the number of cable channels that can be occupied by a video programmer in which a cable operator has an ownership interest ("channel occupancy limits"); and (3) to consider the necessity and appropriateness of imposing limitations on the degree to which "multichannel video programming distributors" may participate in the creation or production of video programming.

3. The MMDS and SMATV cross-ownership restrictions and the anti-trafficking rule contain no specific effective date and thus, pursuant to Section 28 of the 1992 Cable Act, became effective on December 4, 1992 (the effective date of the 1992 Cable Act). However, the provision of the anti-trafficking rule which limits the amount of time that a franchise authority has to disapprove a request to transfer a cable system, will not become effective until the Commission adopts regulations regarding the information required in connection with such requests.[3] The Cable Act of 1992 also requires the Commission to conduct a proceeding to establish subscriber and channel occupancy limits, and to consider the need for establishing limits on the participation of

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[3] 47 U.S.C. § 537(e).

multichannel video program distributors in the creation and production of video programming, within one year from the date of enactment of the 1992 Cable Act (i.e., by October 5, 1993).

4. Neither the 1992 Cable Act nor its legislative history[4] makes plain Congress' rationale in enacting the anti-trafficking rule. The House Report suggests only that Congress intended this provision to restrict profiteering transactions, which are likely to adversely affect cable rates or service in the franchise area[5] In this proceeding, we seek to identify the proper interpretation of the anti-trafficking rule and to establish an appropriate system of implementation.

5. The 1992 Cable Act and its legislative history demonstrate Congress' concern regarding horizontal concentration and vertical integration in the cable television industry. The vertical and horizontal limits required by Section 11 of the 1992 Cable Act are intended to address these concerns. In particular, Congress sought to prevent large, vertically integrated cable systems from creating barriers to entry for new programmers and from causing a reduction in the number of media voices available to consumers. In addition, the 1992 Cable Act was intended to curb the ability and the incentive of cable operators to favor their affiliated programmers over other programming services. Congress also sought to restrict the degree to which vertically integrated program suppliers favor their affiliated cable operators over unaffiliated cable operators and other program distributors.[6]

6. In drafting the 1992 Cable Act, however, Congress also recognized that certain benefits derive from vertical integration and horizontal

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[4]*See* House Committee on Energy and Commerce, H.R.Rep. No. 102-628 ("House Report"), 102d Cong., 2d Sess. (1992); Senate Committee on Commerce, Science and Transportation, S., Rep. No. 102-92 ("Senate Report"), 102d Cong., 1st Sess. (1991); House Committee on Energy and Commerce, H.R.Conf.Rep. No. 102-862 ("Conference Report"), 102d Cong., 2d Sess. (1992).

[5]The House Report also indicates that the anti-trafficking rule was not meant to prevent lenders from obtaining a security interest in connection with providing financing for cable system acquisitions. House Report at 42.

[6]Cable Act of 1992, Sec. 2.

concentration. For example, the House Report acknowledges that vertical relationships promote diversity and make the creation of new, innovative and risky programming services possible[7] Further, the House Report suggests that vertical relationships may be an efficient way of financing new services and compensating cable operators for assuming some of the risk associated with the launch of new cable programming services.[8] With respect to horizontal concentration, the House Report recognizes that consolidation in the cable industry has benefited consumers by allowing efficiencies in administration, distribution, and programming procurement. Further, the House Committee concluded that large multiple system operators ("MSOs") are able to take risks that small operators would not, and that such MSOs provide a sufficient subscriber base to encourage new program entry.[9] In establishing the subscriber limits and channel occupancy restrictions required by the 1992 Cable Act, the Commission must balance the concerns expressed by Congress with the efficiencies and benefits gained by such increased concentration and integration.

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[7]House Report at 41.

[8]*Id.*

[9]*Id.* at 43.

V. SUBSCRIBER LIMITS

29. Seeking to enhance competition in the development, acquisition and delivery of video programming, Section 11 of the 1992 Act requires the Commission within one year to conduct a proceeding to establish horizontal ownership limits. Specifically, Section 11 requires the Commission to "prescribe reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person or in which such person has an attributable interest.[42]

30. In establishing subscriber limits, as well as the other ownership limits mandated by Section 11, the 1992 Cable Act directs the Commission to consider the following public interest objectives of the legislation: (A) to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer; (B) to ensure that cable operators do not favor affiliated video programmers in determining carriage and do not unreasonably restrict the flow of video programming of unaffiliated video programmers to other video distributors; (C) to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise, joint ownership of cable systems and video programmers, and the various types of non- equity controlling interests; (D) to take into account any efficiencies and other benefits that might be gained through increased ownership or control; (E) to ensure that such rules and regulations reflect the dynamic nature of the communications marketplace; (F) to impose limitations that *will not prevent cable operators from serving previously unserved rural areas; and (G) to impose limitations that will not impair the development of diverse and high quality programming.[43] In commenting on the provisions of Section 11, commenters are urged to consider these objectives.

31. The establishment of subscriber limits is intended to address

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[42]47 U.S.C. § 533(f)(1)(A).

[43]47 U.S.C. § 533(f)(2).

Congress' concern regarding increasing horizontal concentration in the cable industry. Horizontal concentration in this context is based on the share of subscribers served by individual cable companies through their ownership or control of local cable systems. The Senate Report noted that TCI, the nation's largest cable operator, serves 14.3 million subscribers (about 24% of the nation's cable subscribers), Time-Warner reaches about 6.4 million subscribers (12% of the nation's subscribers) and the next three largest MSOs, Continental, Comcast and Cox, together control about 5.8 million subscribers (11% of the nation's subscribers).[44] According to information provided to Congress, the top five firms thus serve almost half of the nation's cable subscribers. Congress concluded that this degree of concentration, though low relative to other industries, may enable some MSOs to exercise excessive market power, or monopsony power, in the program acquisition market.[45]

32. In the 1992 Cable Act, Congress found that the increased concentration in the cable industry had the potential to create barriers to entry for new programers and to reduce in the number of media voices available to consumers.[46] Although under traditional antitrust analysis the cable industry is relatively unconcentrated, the 1992 Cable Act requires the Commission to establish limits on the number of subscribers a single entity can reach through cable systems owned by such person.[47] The Conference report is silent regarding what shall consti

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[44]The Committee's statistics are derived from Paul Kagan Associates data and were current as of 1990. More recent data regarding the number of subscribers reached by the 100 largest MSOs can be obtained by reference to Warren Publishing, Inc., Television & Cable Fact Book, Cable & Services Volume No. 59 (Services-Part III), 1992 Edition, p. C-389.

[45]House Report at 42-43.

[46]1992 Cable Act, Section 2(a)(4).

[47]Under the two prevailing measures of market concentration--the four firm concentration ratio ("Four Firm Ratio") and the Hirfindahl-Hirschman Index ("HHI"), the cable industry is not concentrated. The Four Firm Ratio measures the percentage of the

tute reasonable limits for this purpose. The House Report, however, suggests that antitrust analysis should not be the sole measure of concentration in the cable industry.

33. The Commission's own analysis regarding horizontal concentration also concluded that the cable industry has become increasingly concentrated. In its 1990 Report to Congress, the Commission noted that in 1989 the two largest MSOs together served almost 34% of all cable subscribers nationwide, and that the top 10 cable companies served 32.9 million of the nation's 53 million subscribers.[48] We indicated that this degree of concentration among companies that frequently enjoy a monopoly franchise raised "the question of whether MSOs (particularly the largest MSOs) have attained sufficient market power to extract unreasonable concessions from program suppliers and to unfairly restrain competition from alternative distribution services."[49] The Commission also indicated that, on the local level, relatively few cable operators face competition from other multichannel video distributors for either programming or subscribers.[50] In fact, we concluded that it was this level of local concentration that provided MSOs with the potential to take anticompetitive action against programming services

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market captured by the four largest companies in the market. The HHI reflects the distribution of market share among all firms in a given market, giving proportionately greater weight to the market shares of the larger firms. A market is generally considered concentrated when one firm, or a small group of firms, has a sufficient share of the market to exercise power over it. The Justice Department considers an industry concentrated when the HHI exceeds 1800 (although an HHI that exceeds 1000 prompts further evaluation) or when the four firm ratio exceeds 50%. According to the House Report, the HHI for the top 20 MSOs is 491 and the Four Firm ratio for the largest MSOs is 36%, well below the Justice Department's threshold. See House Report at 42.

[48] *Report* in MM Docket No. 89-600, 5 FCCRcd 4962, 5005 (1990) ("1990 Cable Report").

[49] *Id.* at 5003.

[50] *Id.* at 5004.

and competing multichannel providers.[51]

34. On the other hand, the Commission indicated in its 1990 Cable Report that consolidation in the cable industry produced significant benefits and efficiencies to consumers.[52] We noted that higher concentration levels enabled cable companies to take advantage of economies of scale and foster investment in more and better original programming and a wealth of viewing options for consumers. Further, we found that the growth of MSOs had produced significant efficiencies in administration, distribution and procurement of programming which can promote the introduction of new programming services. The Senate Report similarly acknowledged that horizontal concentration may reduce programmers' transaction costs by eliminating the need for negotiation with each of thousands of local cable systems throughout the country.[53] Congress also recognized that horizontal concentration may help promote the introduction of new services into an increasingly competitive programming market by providing capital and a ready subscriber base for such new services.[54]

35. In prescribing subscriber limits, we must, as a preliminary matter, determine the markets in which such subscriber limits should be established. Horizontal concentration may be measured on a local, regional or national basis. The legislative history of the 1992 Cable Act focuses upon the establishment of national subscriber limits, although regional concentration is also mentioned.[55] In the 1990 Cable Report, we concluded that the level of national concentration in the cable

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[51] *Id.* at 5006. In view of our finding in the 1990 Cable Report, we seek comment regarding whether it would be appropriate in calculating compliance with the national subscriber limits to subtract the number of subscribers reached or homes passed by cable systems in areas where effective competition is established.

[52] 1990 *Cable Report* at 5009.

[53] Senate Report at 33.

[54] House Report at 43.

[55] Senate Report at 32-3.

industry was not sufficient to warrant regulatory intervention. We nonetheless indicated that "some cable networks operate on a regional rather than a national basis and an MSO could be sufficiently concentrated to occupy an anticompetitive position at the regional level without possessing a large enough market share to disrupt the national markets."[56] Commenters are asked to indicate whether regional or national subscriber limits, or both, are necessary or appropriate to implement the objectives of the 1992 Cable Act.

36. The Cable Act of 1992 does not define the term "reach" in the context of subscriber limits. Thus, the Commission may prescribe subscriber limits either as a share of cable subscribers or as a share of homes passed. Commenters should address which of these measures should be used to implement the subscriber limits established in this proceeding. We recognize that subscriber-based measures have traditionally been used for purposes of analysis. Nonetheless, we believe that homes passed may be a more appropriate and practical measure for this purpose, since it encompasses all television households for which a particular cable operator provides access to cable programming. Moreover, existing Commission rules applicable to cable/network cross-ownership apply a homes passed measure to implement both national and local subscriber limits.[57] In the Cable/Network Order, we determined that use of a homes passed measure was preferable because a subscriber-based limit could discourage systems from adding new subscribers. We observed that a homes passed measure would be more stable than a subscriber based limit, given the frequent changes in cable subscribership. For the foregoing reasons and to provide consistency in the interpretation of our rules, we tentatively propose to use a homes passed measure to implement

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[56]1990 *Cable Report*, 5 FCCRcd at 5006.A

[57]47 C.F.R. § 76.501 The cable/network restriction was recently relaxed to allow national networks to own cable systems, provided that no such combination exceeds 10% of homes passed by cable nationwide or 50% of homes passed by cable within an ADI. See Report and Order in MM Docket No. 82- 434, 7 FCCRcd 5781 (1992) ("*Cable/Network Order*") (petitions for recon. pending).

the cable subscriber limits established in this proceeding. We seek comment on this proposal.

37. Commenters are also asked to indicate what percentage of homes passed nationally would constitute a reasonable limit on horizontal concentration. Considering the existing market structure and ownership patterns, and the efficiencies and economies of scale resulting from horizontal relationships, we ask whether a limit in the range of 25% to 35% of homes passed would be reasonable or whether some other percentage would be more appropriate. In this regard, commenters should indicate at what percentage of homes passed a single MSO could preclude the success of a new cable service. Are there recent examples of this type of conduct? How many subscribers must be cleared nationally to launch and sustain a new cable programming service? Does the number of subscribers needed vary depending on the type of programming involved? Is it relevant that the Commission's broadcast multiple ownership rules limit the audience reach of television stations in which a person can hold an attributable interest to 25% of television households nationwide.[58] Is it relevant that Commission Rules permit national television networks to own cable systems which reach 10% of the homes passed nationally? This 10% limitation applicable to network-owned cable systems takes into consideration the national audience reach and ability to control programming associated with a broadcast network and, therefore, may not be particularly relevant in the context of crafting national ownership limits for non-network- owned cable systems. It is also important to note that the Senate Report indicates that the 1992 Cable Act was not

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[58]47 C.F.R. § 73.3555. This section also provides for increased ownership of broadcast stations representing up to 30% of the television households nationwide if the additional stations are minority owned. We seek comment on whether we should adopt a similar provision in the cable context. The Commission currently has pending a *Notice of Proposed Rulemaking* in MM Docket No. 91-221 which proposes to relax or eliminate the national audience reach limits applicable to broadcast television. 7 FCCRcd 4111 (1992).

intended to imply that any existing MSO must be divested.[59] Accordingly, commenters are asked to indicate whether divestiture should be required in connection with the subscriber limits we ultimately adopt.

38. The 1992 Cable Act and the Conference Report are silent regarding the appropriate standard for determining ownership of cable systems in connection with application of the subscriber limits. The Senate Report, however, indicates that the Commission should use the attribution criteria set forth in Section 73.3555 (Notes) of our Rules, or such other criteria as the Commission deems appropriate in determining ownership for purposes of applying the subscriber limits.[60] The attribution criteria contained in Section 73.3555 of our Rules may be useful for determining ownership in connection with the subscriber limits we ultimately establish.[61] It should be noted, however, that these attribution criteria were intended to include ownership thresholds which may impart the ability either to influence or control management or programming decisions of a broadcast licensee, and consequently these criteria may not be appropriate to address the concerns at issue in this proceeding. We seek comment regarding whether these attribution criteria (or a modified version thereof) are appropriate for implementing cable subscriber limits or whether some other attribution criteria would be more suitable. In this regard, commenters should also indicate if there are other types of ownership interests, such as non-equity interests, that should be cognizable for purposes of determining ownership under this provision.

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[59]Senate Report at 34. According to the recent data from Warren Publishing, Inc., Television & Cable Fact Book, Cable & Services Volume No. 59 (Services-Part III), 1992 Edition, p. C-389, TCI, the nation's largest MSO, currently reaches 24% of homes passed nationally, and thus it appears that divestiture would not be required if the limit set is within our suggested range of 25% to 30% of homes passed (or higher).

[60]Senate Report at 80.

[61]In the event that we increase the attribution threshold or otherwise modify the attribution criteria as proposed in the Capital Formation Proceeding, commenters should indicate whether we should similarly modify those criteria for purposes of the cable ownership rules.

39. *Jurisdiction and Enforcement.* The 1992 Cable Act does not specifically address how subscriber limits are to be monitored and enforced. In considering this issue it is important to note that presently few if any cable systems are in the range of the proposed subscriber limits. Moreover, subscriber information is publicly available from numerous sources. Consequently, we tentatively conclude that reporting requirements may be unnecessary in connection with enforcing the subscriber limits we ultimately adopt. In the alternative, we believe that a system of certification would be an appropriate means of enforcing the subscriber limits imposed. For example, we could propose requiring cable operators upon transfer or assignment of a cable system to certify that such transfer will not result in ownership of cable systems exceeding the subscriber limits established by the Commission. We seek comment regarding whether such a certification should be made to the local franchise authority, having jurisdiction over the cable system being acquired, or to the Commission. If a system of certification is appropriate, we request comment on whether all cable systems should be required to make the requisite certification or only the five or ten largest cable systems. We also request comment on whether such a certification is necessary at all. Alternatively, we may enforce the subscriber limits on a complaint only basis, pursuant to which parties believing that a particular acquisition would result in a violation of the subscriber limits, would notify the local franchise authority of the acquiring station of the potential violation. We seek comment on these proposals and ask commenters to indicate if there are other more appropriate procedures to enforce the subscriber limits. We also seek comment on whether waivers or exceptions to the subscriber limits should be obtainable in appropriate circumstances. For example, should waivers be granted allowing additional ownership interests for cable systems that expand existing systems to previously unserved rural areas?

40. The Senate Report states that because the cable market is dynamic, the Commission should revisit these limitations at appropriate times to ensure that they continue to accurately reflect the objectives of the

legislation.[62] We believe that periodic review of the ownership limits is important to the continued growth and development of the cable industry. Consequently, we propose to institute a review of the subscriber limits every five years to determine whether such limits are reasonable under the prevailing market conditions. Commenters are asked to indicate whether such review procedures are adequate to ensure that subscriber limits continue to serve the objectives for which they were established.

VI. CHANNEL OCCUPANCY LIMITS

41. Section 11 of the 1992 Cable Act requires the Commission within one year to "prescribe reasonable limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest."[63] Vertical integration in this context refers to common ownership of both cable systems and program networks, channels, services or production companies.

42. In the 1992 Cable Act, Congress concluded that the cable industry has become vertically integrated and that cable operators have the ability and the incentive to favor their affiliated programmers. Such concentration, Congress determined, could make it difficult for non-cable affiliated programmers to secure carriage on cable systems.[64] Similarly, Congress found that, vertically integrated program suppliers also have the incentive and the ability to favor their affiliated cable operators over nonaffiliated operators and program distributors using other technologies.[65] The Senate Report noted that Viacom owns programming services such as MTV, Showtime and Nickelodeon, and that TCI has financial interests in American Movie Classics, the Discovery Channel, QVC and Encore.[66] In addition, the House Report stated

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[62] *Id.* at 80.

[63] 47 U.S.C. § 533(f)(1)(B).

[64] Cable Act of 1992, Section 2(a)(5).

[65] *Id.*

[66] Senate Report at 25.

that according to a study by the National Cable Television Association, 39 of the 68 nationally delivered cable video networks have some ownership affiliation with the operating side of the cable industry.[67]

43. With respect to channel occupancy limits, Congress sought to reduce the incentive and ability of cable operators to favor their affiliated programming services to the disadvantage of unaffiliated programmers. Similarly, Congress intended to discourage vertically integrated programming services from favoring their affiliated cable operators over other cable operators and multichannel video providers. According to the House Report, some vertically integrated MSOs favor programming services in which they have an ownership interest, denying system access to programmers affiliated with rival MSOs. Such vertically integrated MSOs may also discriminate against rival programming services with regard to price, channel positioning, and promotion.[68] In addition, Congress was concerned that vertical integration limits diversity of cable programming and reduces the number of voices available to the public. In this respect, the Senate Report likens the channel occupancy limits to the Commission's broadcast one-to-a-market rule, which are similarly designed to increase the diversity of voices available to the public.[69]

44. On the other hand, the House Report cites a 1988 study by the National Telecommunications and Information Administration ("NTIA"), which concluded that common ownership of cable systems and cable programming services did not appear to affect adversely the supply of cable programming or diversity of viewing choices for cable subscribers.[70] NTIA found that none of the top five MSOs showed a

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[67]House Report at 41.

[68]*Id.* at 43.

[69]Senate Report at 80. The one-to-a-market rule is contained in Section 73.3555 of the Commission's Rules.

[70]House Report at 41, citing *Video Program Distribution and Cable Television: Current Policy Issues and Recommendations*, NTIA Report 88-223, June 1988, p. 102.

pattern of favoring basic services with which they were affiliated. Congress also acknowledged that significant benefits have resulted from vertical relationships in the cable industry. In particular, Congress cited C-Span, CNN, Black Entertainment Television, Nickelodeon, and the Discovery Channel as examples of innovative programming that would not have been feasible without the financial support of cable system operators.[71]

45. In preparing the 1990 Cable Report, we requested and obtained data from nine of the major MSOs regarding the nature and degree of their attributable ownership interests in cable programming services. The data we obtained were current as of December 31, 1989, and are contained in Appendix G to the *1990 Cable Report*.[72] In the 1990 Cable Report, we indicated that TCI owned equity interests in 22 cable networks, Time Warner held interests in eight cable networks and Cox Cable had equity interests in six cable programming services.[73] Overall, we found that MSOs had equity interests in 13 of the top 20 national basic cable networks and in six of the top eight pay cable networks.[74] We concluded that vertical integration had accelerated in the cable industry, but that such vertical relationships had increased both the quality and quantity of cable programming services. We found that MSO investment was responsible for the development and survival of many of the most popular programming services. We also determined that vertical integration of MSOs with significant subscribership has contributed to program diversity by providing new programming services with financial support, an extensive subscriber base and information regarding viewer taste and desire for new programming.

46. The 1992 Cable Act does not indicate the ownership standard that

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[71] *Id.*

[72] *Id.* at 5106-5127.

[73] *1990 Cable Report*, 5 FCCRcd at 5007.

[74] *Id.*

should be applied in connection with channel occupancy limits. The Senate Report indicates that the Committee intended for the Commission to use the attribution criteria set forth in Section 73.3555, or such other criteria as the Commission may deem appropriate in implementing channel occupancy limits. We request comment on whether the attribution criteria contained in Section 73.3555 of our Rules, which are designed to identify ownership interests that afford influence or control over station operations or programming, are appropriate for this purpose. Commenters should indicate whether any modifications should be made for purposes of determining ownership affiliations between cable operators and program services. Commenters are asked to address how application of these attribution rules would affect investment by cable operators in new cable programming services. Parties also are asked to indicate whether higher attribution thresholds are warranted in connection with this restriction in order to provide cable operators with the flexibility to continue investing in new cable programming services.[75]

47. We seek comment on the procedures that should be used in calculating the cable channel occupancy limits we ultimately adopt. The 1992 Cable Act and its legislative history are unclear on this issue. The Senate Report suggests that the Commission may establish such limits based on the number of activated channels, less the number of over-the-air broadcast channels, public, educational, governmental and leased access channels carried. Under this approach, using a hypothetical 20% channel occupancy limit, a system with 54 channels, 14 of which are over-the-air channels, would have a channel occupancy limit of 8 channels for MSO affiliated programming.[76]

48. Parties are requested to comment on whether the procedures for calculating channel occupancy limits outlined in the Senate Report are

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[75]In the event that we increase the attribution threshold or otherwise modify the attribution criteria as proposed in the Capital Formation proceeding, commenters should indicate whether we should similarly modify those criteria for purposes of the cable ownership rules.

[76]Senate Report at 80.

appropriate and reasonably serve the objectives of the legislation. In addressing this issue, commenters should consider that one of the objectives of vertical ownership limits is to ensure that unaffiliated cable programmers have a reasonable opportunity to gain access to vertically integrated cable systems. In this regard, we question whether it is appropriate to subtract the over-the-air broadcast channels and public, educational, governmental and leased access channels in calculating a system's channel capacity. Broadcast channels contain programming that is competitive with cable programming, and leased access channels provide alternative outlets for unaffiliated video programmers. In addition, the commercial and educational broadcast channels are subject to must-carry requirements, pursuant to Section 4 of the 1992 Cable Act. To the extent that carriage of these signals is mandatory, we question whether it is appropriate for such channels to be subtracted from the total number of channels in calculating channel occupancy limits. We seek comment on how such a procedure would serve the statutory objectives of increasing diversity and expanding the number of cable voices available to consumers. We further seek comment regarding how pay channels, such as HBO, Showtime and pay- per-view channels, should be treated for purposes of calculating the channel occupancy limits, since not all subscribers receive these channels. In addition, what provisions should be made for "multiplexing" of pay channels, where the same programming is shown on several different channels at different times? Commenters should also indicate whether channel occupancy limits apply only to vertically integrated national programming networks, or whether such limits should also apply to vertically integrated regional programming networks.

49. It is also unclear from the statutory language and the legislative history how Congress intended such channel occupancy limits to be applied. For example, it is unclear whether such limits were meant to apply only to video programmers affiliated with the particular cable operator or whether such limits were intended to apply to any cable affiliated video programer. It is similarly unclear if the latter interpretation is used, whether the channel occupancy limit should be applied

so that a total of eight channels could be occupied by all vertically integrated programming combined or whether such a limit should be applied so that the programming of each MSO could occupy up to the maximum of eight channels on such a system. The Senate Report could be read to suggest that the channel occupancy limits should apply to the number of channels that any cable operator can devote to any vertically integrated programming, regardless of whether a programmer is affiliated with that particular cable operator.[77] Commenters are asked to indicate how the channel occupancy limits we ultimately adopt should be applied to most effectively address Congress' concerns.

50. Given the uncertainty surrounding the application of the channel occupancy limits, we believe that the more reasoned approach is to apply such limits only to video programmers affiliated with the particular cable operator. We note that such an interpretation would be consistent with Congress' objectives of increasing diversity and expanding the number of voices available to consumers. Moreover, such an interpretation addresses Congress' goal of reducing the ability and the incentive of cable operators' to favor their own affiliated video programmers. Commenters are asked to indicate whether this proposal is appropriate. In considering this issue, commenters should consider whether vertically integrated programing has an adverse effect on diversity. In this regard, we note that, as discussed in paragraph 45, vertical relationships between cable operators and programming services provide essential investment in the development of new programming and enables program producers to spread the risk of developing new and more innovative program services.

51. We also seek comment on how we should determine what constitutes a reasonable channel occupancy limit. What criteria should be used to establish such limits? Are there other regulatory analogies that would be useful in determining what percentage of a cable system's channels should be occupied by vertically integrated program services? In addressing this issue, commenters are asked to consider the vertical

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[77] *Id.*

relationships and ownership patterns that were reported in Appendix G to the 1990 Cable Report. Commenters are asked to provide relevant information, such as the average number of channels occupied by vertically integrated program services. We also request comment on how the availability of leased access channels should affect the establishment of channel occupancy limits. Commenters are asked to indicate the degree to which vertical integration threatens the ability of rival programming services to obtain cable carriage. We note that our intention is to establish a channel occupancy limit that maximizes the number of voices that are available to cable viewers without impairing the ability or incentive of cable operators to invest in new and existing programming services. In this regard, we note that MSO investment has been essential to the development and continuation of many of the most popular and innovative programming services.

52. We tentatively conclude that we should establish a percentage limit on the number of channels that can be occupied by vertically integrated programming services. We ask commenters to indicate what percentage of cable channels would be most appropriate to prevent competitive abuses without discouraging investment relationships between cable operators and program services. In suggesting the appropriate percentage limit, commenters are asked to consider the other structural and behavioral restrictions included in Sections 12 and 19 of the 1992 Cable Act. These restrictions are similarly designed to prevent the adverse effects of vertical integration. Moreover, commenters should consider the must-carry[78] and leased access requirements[79] applicable to cable systems in commenting on this issue.

53. We also seek comment on what effect emerging technologies such as digital signal compression and fiber optic cable should have on the channel occupancy limits. Currently 64% of subscribers receive between 30 and 53 channels, while 28% of cable subscribers receive 54

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[78] 47 U.S.C. § 534.

[79] 47 U.S.C. § 532.

or more channels.[80] Digital compression technology promises to dramatically expand the capacity of existing cable plant. Time Warner is currently testing a cable system with a 150 channel capacity and TCI recently announced plans to introduce a 500 channel system. We believe that such expanded channel capacity will eliminate the need for channel occupancy limits to ensure diversity and prevent discrimination against unaffiliated programming services. Cable systems with such dramatically expanded capacity will require programming from many different sources in order to program so many additional channels. Thus, we propose to establish a threshold beyond which the channel occupancy limits would no longer be applicable. We ask commenters to indicate the appropriate number of total channels for establishing such a threshold. Pursuant to this proposal, the channel occupancy limits would be applied so that a certain percentage of a system's channels could be occupied by vertically integrated programming up to the threshold number of channels, with no limits applicable for channels in excess of the threshold. We believe that this approach is consistent with the objectives of the 1992 Cable Act--to ensure that the regulations prescribed reflect the dynamic nature of the communications marketplace and do not impair the development of diverse and high quality video programming.[81]

54. Finally, we seek comment on whether channel occupancy limits should be phased out in communities where effective competition has developed. Once effective competition has been established and a cable operator no longer occupies a program access bottleneck position, channel occupancy limits may no longer be necessary or desirable. With such developments, the incentive and ability of a cable system to favor its own programming over unaffiliated programming is diminished, and alternative outlets for programming should be available to the public. In seeking comment on this issue, we ask whether

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[80]Warren Publishing, Inc., Television & Cable Fact Book, Cable & Services Volume No. 59 (Services-Part III), 1991 Edition, p. C-389.

[81]47 U.S.C. § 533(f)(2)(E) and (G).

phasing out channel occupancy limits under these conditions is consistent with Congressional intent. In addition, we ask whether channel occupancy limits should be lifted for any cable system that meets the effective competition criteria, or whether only certain of those criteria would justify removing the limits.

55. *Jurisdiction and Enforcement.* The 1992 Cable Act and its legislative history are silent on the issue of enforcement of the channel occupancy limits. We propose that the local franchise authorities have primary responsibility for enforcement of such limits, since they are most familiar with the channel capacity and programming services carried on the systems within their jurisdiction. Because we seek to minimize the burden imposed on local franchise authorities and cable operators by these restrictions, we propose that such channel occupancy limits should be enforced by certification. Accordingly, cable operators would be required to certify annually to the franchise authority that they are in compliance with the channel occupancy limits ultimately adopted. In order to ensure continuous compliance, cable operators would be obligated to notify the franchise authority within 30 days of any changes during the course of the year which would affect compliance with the channel occupancy restrictions. In addition, a franchise authority would be entitled to request any additional information it reasonably determined to be necessary to establish the accuracy of a system's certification, if such certification was challenged. We believe that such a system of certification is appropriate to enforce the channel occupancy limits and will avoid unduly burdening local franchise authorities and cable operators. We also propose to grandfather any existing vertical relationships which exceed the channel occupancy limits at the time such limits are adopted. We believe that divestiture or deletion of programming in connection with implementation of these channel occupancy limits is not required by the 1992 Act and may result in unnecessary disruption of service to the public. We seek comment on this proposal and on whether these procedures are appropriate to ensure compliance with the channel occupancy limits.

FCC 93-456

IN THE MATTER OF
IMPLEMENTATION OF SECTIONS 11 AND 13 OF THE CABLE TELEVISION CONSUMER
PROTECTION AND COMPETITION ACT OF 1992
HORIZONTAL AND VERTICAL OWNERSHIP LIMITS
MM Docket No. 92-264.

Adopted: September 23, 1993 Released: October 22, 1993

SECOND REPORT AND ORDER

By the Commission: Commissioner Barrett issuing a statement.

I. INTRODUCTION

1. In this Second Report and Order ("Report and Order"), the Commission implements Section 11(c)(2) of the Cable Television Consumer Protection and Competition Act of 1992[1] by prescribing national subscriber limits and limits on the number of channels that can be occupied on a cable system by a video programmer in which the cable operator has an attributable interest ("channel occupancy limits"). The Commission declines at this time to impose limits on the degree to which multichannel video programming distributors may engage in the creation or production of video programming as authorized by Section 11(c)(2)(C) of the 1992 Act.[2]

2. We previously issued a Notice of Proposed Rule Making and Notice of Inquiry in this proceeding which sought comment generally on the objectives and scope of Section 11(c)(2) of the 1992 Cable Act.[3] The Notice also asked commenters to address various issues regarding the level at which subscriber limits and channel occupancy limits would be

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[1]Cable Television Consumer Protection and Competition Act of 1992, Pub.L. No. 102-385, 106 Stat. 1460 ("Cable Act of 1992" or "1992 Cable Act").

[2]47 U.S.C. § 533(f)(1)(C).

[3]Notice of Proposed Rule Making and Notice of Inquiry, 8 FCCRcd 210 (1992) ("Notice"). A list of commenters responding to the Notice is provided in Appendix A. These comments were extensively summarized in the Report and Order and Further Notice of Proposed Rule Making ("Further Notice").

reasonable and the appropriate implementation of such limits. In addition, the Commission questioned whether it was necessary or appropriate to adopt limits on the degree to which multichannel video programming distributors ("multichannel distributors") should be permitted to participate in the creation or production of video programming. The Commission subsequently issued a Report and Order and Further Notice of Proposed Rule Making.[4]("Further Notice"), which sought further comment on specific proposals regarding the adoption and implementation of subscriber limits and channel occupancy limits.

3. In summary, this Report and Order contains the following determinations. The Commission establishes a 30% limit on the number of homes passed nationwide that any one entity can reach through cable systems in which such entity has an attributable interest. Horizontal ownership will be determined for this purpose based on the same criteria used by the Commission in the broadcast context. In addition, to promote a diversity of views the Commission will permit ownership of additional cable systems, up to 35% of homes passed nationwide, provided such systems are minority-controlled. However, in view of the recent federal district court decision holding that the Commission's statutory authority to adopt horizontal ownership limits is unconstitutional, and to avoid potential confusion and uncertainty during the period of judicial review the Commission is staying the effective date of the horizontal ownership rules until final judicial resolution of the District Court's decision.[5]

4. With respect to vertical ownership limits, the Commission adopts a 40% limit on the number of channels that can be occupied on a verti-

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[4]Report and Order and Further Notice of Proposed Rule Making in MM Docket No. 92-264, FCC 93-332, released July 23, 1993, ("Further Notice"). A list of commenters responding to the Further Notice and the references to specific commenters used herein is provided in Appendix B.

[5]See Daniels Cablevision v. United States, No. 92-2292 (D.D.C. released September 16, 1993). The vertical ownership limits adopted pursuant to Section 11, which were upheld by the Court are not stayed and will become effective as set forth in para. 109 infra.

cally integrated cable system by video programmers in which the cable operator has an attributable interest. In order to promote a diversity of views the Commission will allow carriage of vertically integrated programming services on two additional channels, or up to 45% of a system's channel capacity, whichever is greater, provided such video programming services are minority-controlled. Vertical attribution is defined for this purpose by reference to the Commission's broadcast attribution criteria. The channel occupancy limits will apply only up to 75 channels. Channel capacity beyond 75 channels will not be subject to vertical ownership restrictions at the present time.

5. The Commission further concludes that in view of the structural and behavioral restrictions already required under the 1992 Act, additional restrictions on the ability of multichannel distributors to engage in the creation or production of video programming are unwarranted at the present. The Commission believes that at the present time the objectives of such a restriction are fully addressed by the vertical and horizontal ownership limits required by Section 11, as well as by the carriage agreement and program access provisions contained in Section 12, and Section 19 of the 1992 Cable Act.

II. BACKGROUND

6. The 1992 Cable Act and its legislative history demonstrate Congress' concern regarding horizontal concentration and vertical integration in the cable television industry. The vertical and horizontal limits required by Section 11 of the 1992 Cable Act are intended to address these concerns. In particular, Congress sought to prevent large, vertically integrated cable systems from creating barriers to entry for new programmers and from causing a reduction in the number of media voices available to consumers. In addition, the 1992 Cable Act was intended to curb the ability and the incentive of cable operators to favor their affiliated video programmers over unaffiliated or competing video programming services. Congress also sought to restrict the degree to which vertically integrated program suppliers favor their affiliated cable operators over unaffiliated cable operators and other program distribu-

tors.[6]

7. In adopting Section 11 of the 1992 Cable Act, Congress also recognized that certain benefits derive from vertical integration and horizontal concentration. For example, the House Report acknowledges that vertical relationships promote program diversity and make the creation of new and innovative programming services possible.[7] Further, the House Report suggests that vertical relationships may be an efficient way of financing new programming services and compensating cable operators for assuming some of the risk associated with the launch of new cable programming services.[8] With respect to horizontal concentration, the House Report recognized that consolidation in the cable industry has benefited consumers by allowing efficiencies in the administration, distribution, and procurement of programming. The House Committee also noted that horizontal concentration may help promote the introduction of new services into an increasingly competitive programming market by providing capital and a ready subscriber base for such new services.[9] The House Report concluded that large multiple system operators ("MSOs") are able to take risks that small operators are not, and that such MSOs provide a large enough subscriber base to facilitate new program entry.[10] The Senate Report similarly acknowledged that horizontal concentration may reduce programmers' transaction costs by eliminating the need for negotiation with individual local cable systems across the country.[11]

8. Recognizing these conflicting factors, Congress directed the Commission to consider and balance the following public interest objectives

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[6]Cable Act of 1992, Section 2.

[7]House Report at 41.

[8]Id.

[9]Id. at 43.

[10]Id.

[11]Senate Report at 33.

in establishing the ownership limits mandated by Section 11: (A) to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer; (B) to ensure that cable operators do not favor affiliated video programmers in determining carriage and do not unreasonably restrict the flow of video programming of affiliated video programmers to other video distributors; (C) to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise, joint ownership of cable systems and video programmers, and the various types of non- equity controlling interests; (D) to take into account any efficiencies and other benefits that might be gained through increased ownership or control; (E) to make rules and regulations that reflect the dynamic nature of the communications marketplace; (F) to impose no limitations that prevent cable operators from serving previously unserved rural areas; and (G) to impose no limitations that will impair the development of diverse and high quality programming.[12]

III. SUBSCRIBER LIMITS

A. Background.

9. Section 11 of the 1992 Cable Act amends Section 613 of the Communications Act to require the Commission to prescribe regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person or in which such person has an attributable interest.[13] The adoption of such ownership limits was meant to address Congress' concerns regarding increasing horizontal concentration in the cable industry.

10. Horizontal concentration in this context is based on the share of subscribers served by individual cable companies through their ownership or control of local cable systems. According to information

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[12]47 U.S.C. § 533(f)(2).

[13]47 U.S.C. § 533(f)(1)(A).

provided to Congress, the top five firms serve almost half of the nation's cable subscribers. Congress concluded that this degree of concentration, though low relative to other industries, may enable some MSOs to exercise excessive market power, or monopsony power, in the program acquisition market.[14] Congress was concerned in particular with preventing large vertically integrated cable systems from creating barriers to entry for new video programmers, and from causing a reduction in the number of media voices available to consumers.[15]

11. Although under traditional antitrust analysis the cable industry is relatively unconcentrated, the 1992 Cable Act requires the Commission to establish limits on horizontal concentration.[16] The Conference Report is silent regarding what shall constitute reasonable limits for this purpose. The House Report, however, indicates that antitrust analysis should not be the sole measure of concentration in the cable industry.[17] The House Report suggests that diversity of information sources can only be assured by imposing limits on the ownership of media outlets that are substantially below those that traditional antitrust analysis would support.

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[14]House Report at 42-43.

[15]1992 Cable Act, Section 2(a)(4).

[16]Under the two prevailing measures of market concentration--the four firm concentration ratio ("Four Firm Ratio") and the Hirfindahl-Hirschman Index ("HHI"), the cable industry is not concentrated. The Four Firm Ratio measures the percentage of the market captured by the four largest companies in the market. The HHI reflects the distribution of market share among all firms in a given market, giving proportionately greater weight to the market shares of the larger firms. A market is generally considered concentrated when one firm, or a small group of firms, has a sufficient share of the market to exercise power over it. The Justice Department considers an industry concentrated when the HHI exceeds 1800 (although an HHI that exceeds 1000 prompts further evaluation) or when the four firm ratio exceeds 50%. According to the House Report, the HHI for the top 20 MSOs is 491 and the Four Firm ratio for the largest MSOs is 36%, well below the Justice Department's threshold. See House Report at 42.

[17]House Report at 42.

12. The Commission's own analysis regarding horizontal concentration also concluded that the cable industry has become increasingly concentrated. In its 1990 Report to Congress, the Commission noted that in 1989 the two largest MSOs together served almost 34% of all cable subscribers nationwide, and that the top 10 cable companies served 32.9 million of the nation's 53 million subscribers.[18] We indicated that this degree of concentration among companies that frequently do not face local competition raised "the question of whether MSOs (particularly the largest MSOs) have attained sufficient market power to extract unreasonable concessions from program suppliers and to unfairly restrain competition from alternative distribution services."[19] The Commission also indicated that, on the local level, relatively few cable operators face competition from other multichannel video distributors for either programming or subscribers.[20] The Commission concluded that it was this level of local concentration that provided MSOs with the potential to take anti-competitive action against video programming services and competing multichannel providers.[21]

13. On the other hand, the Commission indicated in its 1990 Cable Report that consolidation in the cable industry produced significant benefits and efficiencies to consumers.[22] We noted that higher concentration levels enabled cable companies to take advantage of economies of scale and foster investment in more and better original programming and a wealth of viewing options for consumers. Further, the Commission found that the growth of MSOs had produced significant efficiencies in administration, distribution and procurement of programming which can promote the introduction of new video programming

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[18]Report in MM Docket No. 89-600, 5 FCCRcd 4962, 5005 (1990) ("1990 Cable Report").

[19]Id. at 5003.

[20]Id. at 5004.

[21]Id. at 5006.

[22]Id. at 5009.

services.[23] Congress similarly found that such benefits and efficiencies result from increased concentration and instructed the Commission to strike a balance between such benefits and the potential for anti- competitive conduct in determining the appropriate level at which to establish subscriber limits.[24]

B. Applicable Market.

14. Further Notice. In the Further Notice, we proposed to adopt exclusively national subscriber limits and asked commenters to indicate whether national subscriber limits would suffice to implement the objectives of the 1992 Cable Act. With respect to regional limits, we tentatively concluded that the benefits of regional concentration outweigh the potential anti-competitive harm that such concentration may have on the local advertising and programming marketplace. Commenters were asked to address this tentative conclusion.

15. Comments. The majority of commenters addressing this issue favor adoption of exclusively national subscriber limits. Several commenters argue that the 1992 Cable Act does not require or even authorize the Commission to promulgate regional subscriber limits. Moreover, commenters indicate that national limits best serve the objectives of the 1992 Cable Act since most programming distribution occurs on a national, not a regional, basis. These parties add that regional limits would threaten the marketplace efficiencies afforded by regional concentration and would impede the incentive of cable operators to invest in fiberoptic and digital compression technologies that will greatly improve cable service and expand channel capacity. Only INTV supports imposing regional subscriber limits, arguing that such limits are necessary to curb the anti-competitive power of MSOs in local advertising markets.[25] However, numerous commenters respond that

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[23]Id.

[24]House Report at 43; Senate Report at 33.

[25]INTV contends that in markets with only one cable operator, that operator is the conduit for all local advertising and therefore is in the position to dictate local advertis-

there is no evidence that cable operators possess market power in the local advertising or program acquisition markets. These commenters contend that in fact, no such evidence exists because the power of cable operators in these markets continues to lag behind local broadcast stations.[26]

16. Discussion. While we disagree with commenters who assert that the Commission is without authority to adopt regional subscriber limits, we decline to adopt such limits at this time. The Senate Report indicates that even prior to the passage of the 1992 Cable Act the Commission had the necessary authority to adopt horizontal limits at the regional level if it found that such restrictions were warranted.[27] Nevertheless, based on the record in this proceeding and on our interpretation of the 1992 Cable Act, we are persuaded that Congress was primarily concerned with national concentration in the cable industry. While the Senate Report indicates that horizontal concentration "at the regional and national level could present concerns about market power," the Report goes on to say that the FCC is required to establish horizontal ownership limits in order to "address the issue of national concentration in the cable industry.[28] Moreover, Congress' objectives in requiring horizontal ownership limits--to prevent the "concentration of the media in the hands of a few" and to limit the ability of MSOs to exercise undue market power in the program acquisition market--can best be served by

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ing prices, which places other local media (e.g., TV stations) at a considerable disadvantage. INTV Initial Comments at 7-8. In response, cable commenters argue INTV's assertions are disingenuous since data shows that broadcast stations continue to control an overwhelming share of the local advertising market as compared to cable interests. See TCI Initial Reply Comments at 19-20; NCTA Initial Reply Comments at 12-13.

[26]See NCTA Comments at 4-6; Time Warner Comments at 5.

[27]The Senate Report states that "[a]lthough the FCC has the authority to impose horizontal limitations on the cable industry (both national and regional) it has not done so." Senate Report at 34.

[28]Senate Report at 32-34.

the adoption of national subscriber limits. Issues of regional concentration we believe would be better addressed by other provisions of the 1992 Act designed to promote the introduction of competition to established cable franchises.

17. In addition, we find no basis in the record at this point for imposing regional limits that could reduce investment in the development of regional programming, upgraded cable infrastructure and improved customer service. We believe that the potential benefits and efficiencies of regional concentration outweigh any anti-competitive affects in the local programming or advertising marketplace. In fact, the record suggests that cable operators do not possess undue power in the local programming or advertising markets where they face competition from local broadcast stations and other multichannel program distributors. In the absence of record evidence suggesting that any cable operator possesses undue power in the local programming or advertising market, we conclude that it is unnecessary to adopt regional limits at this time.

C. Measurement and Percentage Limitation.

18. Further Notice. The Further Notice proposed to establish subscriber limits as a share of homes passed and sought comment on that proposal. We further proposed to adopt a 25% limit on the number of homes passed by cable systems owned by any one entity, although we continued to seek comment on a limit in the range of 20% to 35% of homes passed. We also asked commenters to indicate whether it would be appropriate in calculating compliance with the subscriber limits to subtract the number of homes passed by cable systems where effective competition--as defined in the 1992 Cable Act--is established. Finally, we asked commenters to address our proposal to allow ownership of additional cable systems, beyond the specified limit, provided such systems are minority-controlled.

19. Comments. All commenters responding to the Further Notice favor measuring the audience reach of cable systems by a homes passed

standard rather than a subscriber-based standard.[29] Most commenters agree that a homes passed standard is more appropriate because a measure based on the number of subscribers is relatively unstable and may have the effect of discouraging subscriber growth.

20. On the issue of establishing a reasonable limit on horizontal concentration, cable commenters continue to advocate a subscriber limit of approximately 30% to 40% of homes passed nationwide.[30] These commenters argue that the record does not support the Commission's proposal to adopt a 25% ownership limit. In addition, these commenters assert that in the absence of empirical evidence that existing levels of concentration afford cable operators undue power in the programming market, the Commission should establish subscriber limits significantly above 25%. NCTA, TCI and Time Warner also support allowing additional investments in cable systems beyond the proposed limit provided such cable systems are minority-controlled.[31] TCI suggests that all investments in minority-controlled cable systems should be exempt in order to encourage MSOs to invest in a large number of minority-controlled cable systems. According to these commenters, such ownership incentives will increase minority ownership of cable systems and promote programming diversity.

21. Cable commenters contend that the record indicates that cable

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[29]See NCTA Comments at 9; Liberty Media Initial Comments at 32; NATOA Comments at 14; Discovery Comments at 8-9; MPAA Comments at 2; INTV Initial Comments at 4; TCI Initial Comments at 28-29. Time Warner continues to advocate its earlier proposal that horizontal limits should be measured as fraction which has (a) as its numerator, the number of cable subscribers served by a particular cable operator; and that has (b) as its denominator, the sum of (i) the number of all cable subscribers nationwide and (ii) the number of subscribers served by other multichannel video programming distributors. However, Time Warner concurs with the Commission's proposal to measure horizontal ownership as a share of homes passed nationwide. Time Warner Comments at 9-10.

[30]See Liberty Media Comments at 9; NCTA Comments at 7-8; TCI Comments at 13-17; Time Warner Comments at 7-8; Discovery Initial Comments at 9.

[31]See NCTA Comments at 9; TCI Comments at 18; Time Warner Comments at 7- 8.

systems with a 30% to 40% share could not preclude the launch or success of new video programming services and that establishing ownership limits below this level will impede the development of new cable technologies. Moreover, cable commenters rely on antitrust principles to argue that MSOs must have at least a 50% market share in order to be regarded as having market power. Cable commenters further assert that the program access, must carry, leased access and rate regulation provisions of the 1992 Cable Act already prevent the abuses Congress was concerned might result from excessive horizontal concentration and therefore the structural limits imposed by subscriber limits need not be overly restrictive. Finally, cable commenters contend that adoption of a 25% limit will stifle investment in new cable programming and the development of new technologies because cable operators will not have adequate advertising revenues and subscriber fees to reinvest.

22. In support of their position that a 30% to 40% subscriber limit is reasonable, cable commenters add that extensive subscriber penetration is not essential to the success of a new programming network. Time Warner, TCI and NCTA observe that many cable programming services have flourished at subscriber penetration levels well below 60%.[32] Therefore, these commenters contend that there is no basis on which to conclude that an MSO with a 30% to 40% market share can impede the success of new video programming services.

23. In contrast to the cable commenters, MPAA continues to advocate

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[32]These commenters note that program networks such as Black Entertainment Television, The Learning Channel, Bravo and Court TV have had achieved success with penetration levels of less than 30% to 40%. See Time Warner Comments at 7-8; TCI Comments at 17; NCTA Comments at 7. In addition, Time Warner notes that The Family Channel, which was launched in 1977 achieved less than 10% penetration of all cable homes by its second year of operation, achieved only 22.1% in its third year, but approached 60% penetration by its sixth year of carriage. Another example provided by Time Warner is Nickelodeon, which achieved only 15.1% penetration in its second year of operation and now enjoys over 90% penetration. Time Warner Initial Comments at 27-28.

a 25% subscriber limit. MPAA argues that a limit of 25% of homes passed is reasonable because it does not require divestiture and would in fact allow most cable operators to expand. MPAA also contends that there are no compelling public interest factors which support a subscriber limit higher than 25%. MPAA asserts that higher levels of concentration are not necessary to induce cable operators to invest in the development of advanced cable technologies, and cites numerous examples of cable companies, with subscriber levels below six percent, who have committed to major investments in the deployment of advanced cable technologies.[33] NATOA similarly supports the 25% limit proposed in the Further Notice, arguing that any higher limit would be inadequate to serve Congress' objectives and would allow cable operators to preclude the success of new or competing video programming services by denying them access to an adequate subscriber base to develop the necessary level of viewership.[34]

24. Discussion. The language of Section 11(C)(2)(A) speaks of establishing limits on "the number of cable subscribers" any one person can reach through cable systems owned by such person. We believe that the term "reach" can be reasonably construed to mean the share of homes passed by a cable operator. Such a measure necessarily encompasses all potential cable subscribers and constitutes a more stable basis on which to impose horizontal limits. Moreover, this interpretation would more adequately reflect a cable operator's potential reach, by encompassing all of the cable homes to which a particular cable operator controls access.[35]

25. In adopting ownership limits we seek to balance two competing

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[33]See MPAA Comments at 3.

[34]See NATOA Comments at 13-14.

[35]The Commission similarly employs a homes passed measure to implement the revised network/cable cross-ownership restrictions. See Second Report and Order in MM Docket No. 82-434 (Elimination of Prohibition on Network Cable Cross-Ownership) 7 FCCRcd 1 (1992).

concerns raised by Congress: on the one hand, the possibility that large horizontally integrated MSOs might have the ability to preclude the launch of new video programming services and on the other hand, the benefits and efficiencies that result from greater horizontal concentration.[36] Based on our consideration of these statutory factors and on the preponderance of the data provided in the record, we conclude that a horizontal ownership limit prohibiting any one entity from having an attributable interest in cable systems that in the aggregate reach more than 30% of cable homes passed nationwide strikes the proper balance. A 30% horizontal ownership limit is generally appropriate to prevent the nation's largest MSOs from gaining enhanced leverage from increased horizontal concentration. Nonetheless, it also ensures that the majority of MSOs continue to expand and benefit from the economies of scale necessary to encourage investment in new video programming services and the deployment of advanced cable technologies.

26. We believe that this 30% limit is reasonable to prevent the types of anti- competitive conduct which concerned Congress, particularly when coupled with the behavioral restrictions contained in Sections 12 and 19 of the 1992 Cable Act, which are similarly intended to prevent cable operators from exercising undue power vis-a-vis video programmers and consumers.[37] Moreover, Sections 4 and 5 require cable operators to carry the signals of local commercial and non-commercial broadcast stations. The vertical ownership limits adopted herein and Section 612 of the Communications Act also require cable systems to make a specified percentage of channels available to unaffiliated programmers,

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[36]See para. 7 supra.

[37]Specifically, the restrictions required by Section 12 are designed to prevent cable operators, as well as other multichannel video program distributors, from requiring a financial interest or exclusive rights in a video programming service as a condition of carriage. In addition, Section 19 of the 1992 Cable Act prohibits vertically integrated cable operators from engaging in unfair or deceptive acts or practices the purpose or effect of which is to hinder significantly or to prevent any multichannel video programming distributor from providing programming to consumers.

which ensures that a diversity of views are presented to cable subscribers. The cumulative effect of these regulations coupled with a horizontal ownership limit of 30% should protect against any one cable system exerting undue power that could prevent the success of new video programming services or "unfairly impede the flow of video programming to the consumer.[38] We also believe that this limit combined with the above mentioned provisions will be appropriate to address the diversity aims which underlie the statutory horizontal ownership provisions. At the same time such a limit will allow the majority of cable operators to expand their system ownership and avail themselves of any efficiencies and other benefits which might be gained through increased ownership or control of cable systems.[39]

27. While we proposed a 25% horizontal ownership limit in the Further Notice, we sought comment on a range of 20% to 35%. In concluding that a 30% limit was reasonable we considered a number of factors including the indication in the legislative history of this provision that Congress did not intend necessarily to require the divestiture of any existing interests.[40] In this regard, the Senate Report states that "[t]he legislation does not imply that any existing company must be divested and gives the FCC flexibility to determine what limits are reasonable."[41] Thus, we determined that in the absence of definitive evidence that

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[38]47 U.S.C. § 533(f)(2)(A).

[39]47 U.S.C. § 533(f)(2)(D).

[40]We note in this regard that the largest existing MSO, TCI, using the attribution standards adopted herein, has an interest in cable systems passing approximately 23.8 million homes or 27% of homes passed nationwide. See TCI submission dated September 22, 1993. This number is larger than the number used for corporate and other reporting requirements because, inter alia, it includes systems in which an "attributable interest" is held rather than systems that are treated as "consolidated for certain corporate and other reporting purposes. Compare, Television Digest, June 7, 1993, p. 4 (TCI and consolidated subsidiaries in which the ownership interest is greater than 50% as of December 31, 1992, pass 17.7 million homes).

[41]Senate Report at 34.

existing levels of ownership are sufficient to impede the entry of new video programmers or have an adverse affect on diversity, existing arrangements should not be disrupted. Based on our review and consideration of the record, we are persuaded that such divestiture is unnecessary. There is ample support in the record for a limit of at least 30%. Moreover, we believe that a 30% limit in conjunction with other provisions of the 1992 Cable Act is reasonable to prevent cable operators from creating barriers to the entry of new video programmers without unduly restricting their ability to reach their desired audience. Such a limit will also enable cable operators to avail themselves of the benefits and efficiencies of horizontal concentration and may provide an incentive for MSO investment in upgraded technology and infrastructure.

28. As we proposed in the Further Notice, in order to encourage a diversity of viewpoints we will allow ownership of additional cable systems reaching up to 35% of cable homes passed, provided such additional cable systems are minority-controlled. The Commission has long supported increased minority participation and ownership in the cable industry, believing that such minority ownership is a significant means of fostering the inclusion of a diversity of views in cable programming.[42] We are convinced that the minority ownership incentive we adopt today in connection with the horizontal ownership limits will be an important means of furthering this goal by encouraging MSO investment in minority-owned cable systems, which in turn will promote additional minority ownership of cable facilities and greater minority participation in the selection of programming. We believe that the increased diversity that this additional minority ownership will encourage outweighs the marginal impact on competition that could result from the increased concentration. Notably, we provide a similar incentive

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[42]See Policy Statement on Minority Ownership of Cable Television Facilities, 52 RR 2d 1469, 1471 (1982) (expanding Commission's tax certificate policy to include sales and exchanges of cable television facilities in order to encourage minority ownership of cable facilities).

in the broadcast context to increase the diversity of programming.[43]

29. We decline to calculate compliance with the national subscriber limits by subtracting the number of homes passed by cable systems in areas where effective competition is established. The statutory provisions and the implementing rules we are adopting focus on ensuring that system operators are constrained in terms of the total share of the market they may occupy in order that no single operator exerts an undue influence, particularly at the national level, on the diversity of programming services available through cable television. The presence of competition in particular markets ameliorates some of the concerns involved and provides members of the public in those markets with the opportunity, through the competitor they select, to influence directly the services offered in those markets. The presence of effective competition in any given system or group of systems does not, however, directly respond to Congress' concern about the exercise of undue control by a single entity at the national level.

D. Horizontal Attribution Standard.

30. Further Notice. In the Further Notice we proposed to adopt the broadcast attribution standard to implement horizontal ownership limits and asked commenters to indicate whether this standard was appropriate. We indicated that since these same attribution criteria are used to implement the broadcast multiple ownership rules and cable cross-ownership rules, which have similar objectives, it would appear that they are also appropriate in the context of cable subscriber limits.

31. Comments. Cable commenters generally advocate an attribution standard based on actual control which they contend is more appropriate in determining the ability of a cable operator to control the programming decisions of a particular system.[44] While these commenters recognize that control may be exerted by less than a majority interest, they nevertheless assert that 5% is far too low a standard. NCTA advocates a 20%

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[43]See 47 C.F.R. § 73.3555(e)(1).

[44]See NCTA Comments at 10-11; Time Warner Comments at 13; Liberty Media Initial Comments at 17.

attribution threshold and Time Warner favors a 25% equity threshold.

32. TCI continues to advocate an attribution standard that would (1) exempt ownership interests under 10% ownership; (2) attribute interests of 50% or more; and (3) prorate interests between 10% and 50% based on the number of subscribers served by the system.[45] Generally, TCI and the other cable commenters oppose adoption of the broadcast attribution criteria in this context arguing that such a strict standard is inappropriate because a 5% interest holder is incapable of influencing a cable system's program choices.[46]

33. On the other hand, MPAA, ABC, E! Entertainment, Turner and BET support the use of the broadcast attribution criteria. Specifically, MPAA observes that these criteria have worked well in the broadcast area and were suggested in the legislative history as the appropriate criteria to used in the cable context.[47]

34. Discussion. We believe that the broadcast attribution criteria contained in Section 73.3555 of the Commission's rules are appropriate to implement the horizontal ownership limits.[48] Pursuant to these criteria, all voting stock interests of 5% or more are attributable. Non-voting stock interests (including most "preferred" stock classes) are not attributable. There are several exceptions to the presumption of attribution created by the 5% benchmark. Most notably there is a single majority shareholder exception, which provides that minority interests

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[45]See TCI Comments at 19-24. TCI would also incorporate a single majority shareholder exception as is used in the broadcast context. Id.

[46]See Time Warner Comments at 13. Time Warner also contends that Congress did not intend for the Commission to adopt such a strict attribution standard, noting that the Senate Report that preceded the 1992 Cable Act mentioned the broadcast standard under Section 73.3555 as a possible model for developing attribution criteria. Id.

[47]See MPAA Comments at 6.

[48]For the sake of convenience, the actual rules now being adopted reference the standards set forth in the notes to Section 76.501 of the rules (cable ownership rules). These are derived from and are not substantively different from those generally referred to as the broadcast attribution rules, i.e., Section 73.3555.

will not be attributed where there is a single 51% shareholder. In addition, the interests of "insulated" limited partners are not attributed.

35. In employing the Section 73.3555 attribution criteria for this purpose, we note that the objectives of the broadcast attribution model are consistent with our goals in establishing ownership standards for subscriber limits. In this regard, the broadcast attribution rules focus on ownership thresholds that enable a broadcast licensee to influence or control management or programming decisions. We believe these same issues are also relevant to addressing the concerns at issue in this proceeding relating to the ability of cable operators to unduly influence the programming marketplace. We also note that the legislative history of the 1992 Cable Act supports the use of the broadcast attribution criteria.[49]

E. Enforcement.

36. Further Notice. The Further Notice asked commenters to address how compliance with the subscriber limits should be monitored and enforced. We indicated that since few cable systems were in the proposed range of 20%-35%, a certification process may be appropriate to enforce such limits. We suggested that cable operators reaching 20% of homes passed could be required upon transfer or assignment of a cable system to certify that the transfer or sale of such system would not violate the subscriber limits. Alternatively, we noted that such certification may be unnecessary if the Commission could monitor horizontal concentration by reference to publicly available information. We asked commenters to indicate what sources are publicly available that would enable the Commission to monitor horizontal concentration according to the number of homes passed by the largest cable systems. We also asked commenters to indicate if the Commission should consider waivers of the subscriber limits in appropriate cases and whether the

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[49]See Senate Report at 80. The Senate Report indicates that the Commission should use the attribution criteria set forth in Section 73.3555 (Notes) of our Rules, or such criteria as the Commission deems appropriate in determining ownership under the subscriber limit regulations.

Commission should periodically review the subscriber limits to determine their continuing relevance.

37. Comments. MPAA and most cable commenters support the proposed system of certification to enforce subscriber limits. NCTA and Time Warner, however, indicate that the Commission need not institute a certification process to enforce the subscriber limits since so few companies are near the proposed limits. NCTA suggests that the Commission can readily obtain information regarding the number of cable homes passed using data from Kagan Associates or Cable Television Financial Data, which are relied upon by the industry for subscriber information according to homes passed. Alternatively, TCI and Liberty Media advocate complaint-based enforcement.

38. Time Warner and NCTA also suggest that the Commission should consider waivers in appropriate cases such as for expansion of service into previously unserved rural areas and for de minimis violations (e.g., when commercial circumstances temporarily place an operator over the limits).[50] In addition, MPAA, Time Warner and NCTA favor the Commission's proposal to review the subscriber limits every five years.[51]

39. Discussion. We conclude that in order to enforce most efficiently and effectively the horizontal ownership limits, we should institute a system of certification. Although public information is available from various sources regarding the number of homes passed by the largest cable operators, such sources generally apply different attribution criteria than the Commission has decided to employ. Therefore, we will require entities holding attributable interests in cable systems reaching 20% or more of homes passed nationwide to certify to the Commission, prior to the acquisition of any additional cable systems, that such acquisition will not result in a violation of the horizontal

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[50] See Time Warner Comments at 14; NCTA Comments at 12-13.

[51] See MPAA Comments at 2 & 6-7; Time Warner Comments at 14; NCTA Comments at 13.

ownership limits adopted herein.[52] Where a transaction will result in a cable operator exceeding the limit, the cable operator must seek either a permanent or temporary waiver from the Commission, which might also include a commitment to divest a sufficient number of systems so as to come into compliance with these ownership limits after the acquisition is completed. The Commission will consider waiver requests only in limited circumstances where an acquisition temporarily places a cable operator over the permissible number of subscribers or where an MSO seeks to expand service into an otherwise unserved rural area.

40. Finally, in view of the fact that the cable television industry is so dynamic and fluid, we believe that periodic review of the ownership limits is necessary. As we proposed in the Further Notice, we plan to review the subscriber limits every five years to determine whether such limits are reasonable under the prevailing market conditions and whether such limits continue to serve the objectives for which they were adopted. We regard such periodic review as ~~an~~ important means of addressing Congress' intent that such rules reflect the "dynamic nature of the communications marketplace."[53]

IV. CHANNEL OCCUPANCY LIMITS

A. Background

41. Section 11 of the 1992 Cable Act also requires the Commission to establish reasonable limits on the number of cable channels that can be occupied by a video programmer in which a cable operator has an attributable interest.[54] Congress adopted this provision to address its concerns that the cable industry has become increasingly vertically integrated and that as a result cable operators have the ability and the

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[52]We contemplate that the MSO whose aggregate attributable interests in cable systems equals or exceeds 20% of homes passed nationwide will be responsible for filing the requisite certification. Thus, if a system in which TCI holds an attributable interest acquires an additional cable system, TCI will be the party responsible for certifying to the Commission that the transaction will not result in a violation of FCC rules.

[53]47 U.S.C. § (f)(2)(E).

[54]47 U.S.C. § 533(f)(1)(B).

incentive to favor their affiliated programmers over unaffiliated or competing distributors. Vertical integration in this context refers to common ownership of both programming and distribution systems. Such integration, Congress determined, could make it difficult for non-cable affiliated or competing programmers to secure carriage on vertically integrated cable systems.[55] Congress similarly found that vertically integrated program suppliers have the incentive and the ability to favor their affiliated cable operators over unaffiliated operators and program distributors using other technologies.[56]

42. According to the House Report, some vertically integrated MSOs favor video programming services in which they have an ownership interest, denying system access to unaffiliated programmers and programmers affiliated with rival MSOs. The House Report also found that such vertically integrated MSOs may discriminate against rival video programming services with regard to price, channel positioning, and promotion.[57] In addition, Congress was concerned that vertical integration limits diversity of cable programming and reduces the number of voices available to the public. In this respect, the Senate Report likens the channel occupancy limits to the Commission's broadcast one-to-a-market rule, which is similarly designed to increase the diversity of voices available to the public.[58]

43. On the other hand, the House Report cites a study by the National Telecommunications and Information Administration ("NTIA"), which concluded that common ownership of cable systems and cable programming services did not appear to affect adversely the supply of cable

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[55]Cable Act of 1992, Section 2(a)(5).

[56]Id.

[57]House Report at 43.

[58]Senate Report at 80. The one-to-a-market rule is contained in Section 73.3555 of the Commission's rules.

programming or diversity of viewing choices for cable subscribers.[59] NTIA found that none of the top five MSOs showed a pattern of favoring basic services with which they were affiliated. Congress also acknowledged that significant benefits have resulted from vertical relationships in the cable industry. In particular, the House Report cited C-Span, CNN, Black Entertainment Television, Nickelodeon, and the Discovery Channel as examples of innovative programming that would not have been feasible without the financial support of cable system operators.[60]

44. In the 1990 Cable Report, the Commission also found that the cable industry had become vertically integrated. In this regard, the Commission observed that MSOs had equity interests in 13 of the top 20 national basic cable networks and in 6 of the top 8 pay cable networks.[61] We concluded that vertical integration had accelerated in the cable industry, but that such vertical relationships had increased both the quality and quantity of cable programming services. We found that MSO investment was responsible for the development and survival of several of the most popular video programming services. We also determined that vertical integration among the largest MSOs had contributed to program diversity by providing new video programming services with an extensive subscriber base and information regarding viewer tastes and desires for new programming.

45. As with the establishment of horizontal ownership limits, we seek to establish channel occupancy limits which strike the proper balance between competing statutory objectives: to ensure that vertically integrated cable operators do not favor affiliated video programmers, or unfairly impede the flow of video programming to cable subscribers, on the one hand and, on the other, to encourage MSOs to continue to

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[59]House Report at 41, citing Video Program Distribution and Cable Television: Current Policy Issues and Recommendations, NTIA Report 88-223, June 1988, p. 102.

[60]House Report at 41.

[61]Cable Report at 5009.

invest in the development of diverse and high quality video programming services.[62] Congress expressly indicated that the Commission should "not impose limitations which would impair the development of diverse and high quality programming."[63]

B. Application of Channel Occupancy Limits.

46. Further Notice. In the Further Notice we indicated that the statutory language and legislative history were unclear regarding how Congress intended such channel occupancy limits to be applied. In particular, we noted that we were uncertain whether Congress intended such limits to apply only to video programmers affiliated with the operator of the particular cable system in question or whether such limits were intended to apply to carriage of all cable affiliated video programming on all cable systems. We also questioned whether in calculating a system's channel capacity we should subtract the number of broadcast, PEG and leased access channels.

47. Given the ambiguity, we proposed to apply such limits only to video programmers affiliated with the particular cable operator. We noted that such an interpretation would be consistent with Congress' objectives of increasing diversity and expanding the number of voices available to consumers. Moreover, we observed that such an interpretation would address Congress' goal of reducing the ability and the incentive of cable operators to favor their affiliated video programmers. We also proposed to include all activated channels including broadcast, PEG and leased access channels in calculating system capacity.

48. Comments. Cable commenters assert that the statutory language and the purpose of the legislation make clear that Congress intended for such limits to apply only to video programming services affiliated with the particular cable operator.[64] According to these parties, cable opera

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[62] See para. 7 supra.

[63] 47 U.S.C. § 533(f)(2)(G).

[64] See NCTA at Comments 13-14; Turner Comments at 6; Cablevision Systems Initial Comments at 10; TCI Initial Comments at 35-36; Time Warner Initial Comments at

tors have no incentive to favor a video programmer affiliated with a rival MSO. Nor do they have the ability to influence the programming content of such unaffiliated video programming services. Several commenters also assert that the establishment of channel occupancy limits raises serious First Amendment concerns that will be exacerbated by an unnecessarily broad application of such limits to carriage of all affiliated video programming services on all cable systems.[65]

49. Most commenters also agree that the Commission should take into account all activated channels, including all broadcast, PEG and leased access channels, in calculating system capacity.[66] These commenters note that such channels provide unaffiliated and diverse programming that is competitive with affiliated programming. According to cable commenters, subtracting broadcast, PEG, and leased access channels is unwarranted as a policy matter and would penalize cable operators who carry the broadest array of broadcast, PEG and leased access channels by reducing the channel base available for carriage of affiliated video programming services.

50. In contrast, NATOA contends that the FCC should subtract all broadcast, PEG and leased access channels in calculating channel

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45-48; IFE Initial Comments at 7-9; Liberty Media Comments at 13; E! Entertainment Initial Commentsat 7; Discovery Comments at 5; and Viacom Comments at 7-8; CIC/CC Initial Comments at 35-37. Commenters cite to language in the Conference Report stating that the Commission shall adopt reasonable limits on the "number of channels that can be occupied by a programmer that is owned by a cable operator or in which the cable operator has an attributable interest." Conference Report at 81 (emphasis added).

[65]See Time Warner Initial Comments at 2; Turner Comments at 4; Viacom Initial Comments at 2-3; NCTA Initial Comments at 24; TCI Initial Comments at 29; CIC/CC Initial Comments at 35; Cablevision Systems Initial Comments at 9-10; Liberty Media Initial Comments at 12, n. 5.

[66]See NCTA Comments at 14; Turner Comments at 5; Viacom Comments at 5-8; Time Warner Initial Comments at 41-42; Discovery Comments at 6; CIC/CC Initial Comments at 39-40; Liberty Media Comments at 13-14; MPAA Comments at 9.

capacity.[67] NATOA maintains that the legislative history indicates that Congress intended such channels to be subtracted prior to application of the channel occupancy limits.[68] NATOA also notes that adherence to this procedure would yield more channel capacity for unaffiliated programmers.[69]

51. Discussion. Section 11(c)(2)(B) requires the Commission to "establish reasonable limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest."[70] The language contained in Section 11(c)(2)(B) of the 1992 Cable Act is not entirely clear because it can also be read as applying to carriage of video programmers affiliated with the particular cable operator or to carriage of any vertically integrated cable programmer on any cable system. However, the Conference Report specifies that such limits shall apply to "the number of channels that can be occupied by a video programmer that is owned by a cable operator or in which the operator has an attributable interest."[71]

52. We thus agree with the majority of commenters who assert that the most logical interpretation of the statutory language is to apply such

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[67]See NATOA Comments at 21. See also INTV Initial Comments at 11;

[68]The Senate Report states in relevant part that

"The intent of this provision is to place reasonable limits on the number of channels that can be occupied by each MSO's programming services. For example, the FCC may conclude that each MSO should control no more than 20 percent of the channels on any cable system, with a minimum of 6 channels being permissible. The FCC should establish these rules based on the number of activated channels less the numbers of over-the-air broadcast signals carried and the number of public, educational and governmental and leased access channels carried. On a system with 54 channels, 14 of which are occupied by over-the-air signals or access channels, the limit then would be eight channels that could be occupied by programming owned by an MSO...." Senate Report at 80.

[69]See NATOA Comments at 7.

[70]47 U.S.C. § 533(f)(1)(B) (emphasis added).

[71]Conference Report at 81 (emphasis added).

limits only to video programmers that are vertically integrated with the particular cable operator in question. We believe that this represents the most reasoned approach given Congress' stated objective of encouraging a diversity of voices and preventing unaffiliated programmers from being denied carriage on vertically integrated cable systems.

53. We agree that cable operators have very little incentive to favor video programming services that are affiliated solely with a rival MSO. Moreover, a vertically integrated cable operator appears to have significantly less power to control the content or distribution of a programming service in which it has no ownership interest. Further, we believe that application of the channel occupancy limits to all vertically integrated programmers, regardless of whether they are affiliated with the particular cable operator, would severely inhibit MSO investment in video programming services, since the mere fact of such MSO investment may restrict carriage of the video programming service on all cable systems. In the absence of significant empirical evidence of existing discriminatory practices, we see no useful purpose in limiting the ability of cable operators to carry programming affiliated with a rival MSO. Such a restriction would be unduly burdensome on MSO investment in cable programming and would be contrary to the purpose of the statute. Moreover, we seek to adopt reasonable carriage limits that will balance both the benefits and concerns associated with vertical integration.

54. With respect to calculating channel capacity, we conclude that all activated channels should be taken into account. We note that cable operators are obligated by the 1992 Cable Act to carry local broadcast and noncommercial educational channels, and are required to reserve channel capacity for lease to unaffiliated programmers. Consequently, we conclude that it would be unreasonable to use such channels to reduce the base of channels available for carriage of vertically integrated programming. We believe that the such an approach would penalize cable operators who carry the broadest array of broadcast channels by decreasing the number of channels available for carriage of vertically integrated programming. In addition, we note that there is precedent for including all channels in the calculation of channel capacity in the

must carry and leased access provisions of the Communications Act, which take into account all activated channels in determining a cable operator's carriage obligations.[72] Moreover, carriage of broadcast, PEG and leased access channels promotes diversity and provides alternative sources of unaffiliated programming to cable subscribers in furtherance of the statutory objectives. In this regard, we disagree with NATOA's argument that the legislative history requires that the Commission subtract all broadcast, PEG and leased access channels prior to application of the channel occupancy limits. The Senate Report language relied upon by NATOA appears to be included merely as an example to illustrate how the Commission may decide to calculate channel occupancy limits and therefore does not prohibit the Commission from adopting an alternative approach if it finds such an approach to be reasonable to promote the legislative objectives. In any event, this language is not included in the statute itself.

55. Finally, we address the arguments advanced by some commenters that the channel occupancy provisions of the 1992 Act violate the First Amendment. At the outset, it should be noted that the Commission has an obligation to execute and enforce the provisions of Section 11 enacted by Congress and therefore is not free to declare an act of Congress unconstitutional.[73] Nevertheless, we believe that the statute is constitutional. We note that Congress, in enacting the cable access provisions under the Cable Communications Policy Act of 1984, P.L. 98-549, and the cable must carry obligations under the 1992 Cable Act, carefully considered the First Amendment rights of cable operators and others and concluded that these provisions were constitutionally permissible as consistent with and in furtherance of the goals of the First

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[72]47 U.S.C. §§ 532, 534.

[73]See Johnson v. Robinson, 415 U.S. 361, 368 (1974) and Meredith Corp. v. FCC, 255 U.S.App.D.C. 22, 31 (D.C.Cir.1987).

Amendment.[74] We believe that the channel occupancy limits provided in Section 11 are generally analogous to the cable access and must carry provisions and, similarly, do not believe that these limits infringe the First Amendment rights of cable operators or others. Moreover, we note that the federal district court in Daniels Cablevision, Inc. v. United States, which struck down the subscriber limit authority in Section 11, upheld other provisions of the 1992 Cable Act in dispute, including the Section 11 channel occupancy limits, as "facially compatible with the First Amendment."[75]

C. Vertical Ownership Attribution Standard.

56. Further Notice. The Further Notice proposed to employ the broadcast attribution criteria for purposes of determining vertical integration in the context of channel occupancy limits. Commenters were asked whether these criteria were appropriate or whether a higher attribution standard would be appropriate to encourage continued MSO investment in cable programming. We also asked commenters to indicate whether a higher equity threshold should be adopted where more than one MSO holds a non-controlling interest in a video programming service.

57. Comments. Commenters addressing this issue propose a variety of vertical integration standards. NCTA and most cable commenters

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[74]See H.R.Rep. No. 934, 98th Cong., 2d Sess. at 31-36 (1984) and H.R.Rep. No. 628, 102d Cong., 2d Sess. 58-67 (1992). Indeed, although subject to further review by the U.S. Supreme Court, the cable must carry provisions of the 1992 Act were recently upheld as constitutional as against First Amendment challenges by cable operators and others. Turner Broadcasting System, Inc. v. FCC, 819 F.Supp. 32 (D.D.C.1993) (three-judge court).

[75]The Court in Daniels Cablevision, Inc. said that "the channel occupancy limits appear unrelated to content" but added:

Whether or not the regulations ultimately promulgated by the Commission will pass constitutional muster under O'Brien/Ward is, of course, at this point unclear.

Slip op. at 13. We believe the specific regulations adopted here would meet the O'Brien/Ward test. See United States v. O'Brien, 391 U.S. 367 (1968) and Ward v. Rock Against Racism, 491 U.S. 781 (1989).

favor an ownership criteria based on control, which they define as either majority voting control or the ability to elect a majority of the board of directors.[76] Discovery argues that if integration is defined as less than control, the regulations should include a behavioral exception which, if satisfied, would exempt affiliated video programming service from attribution.[77]

58. MPAA proposes an attribution threshold of 15% (combined with a lower channel occupancy limit) to implement Section 11. MPAA notes that this standard differs from the attribution criteria they recommend in connection with subscriber limits. However, they believed that such a distinction is warranted by marketplace circumstances. In this regard, MPAA observes that it is common for a large number of cable operators to each take a minority position in a programmer, thus spreading control more widely among operators. According to MPAA, such participation by a number of different MSOs warrants a higher attribution level than is applied in cable system ownership, where one MSO generally controls management and operations decisions, including program selection.[78]

59. TCI suggests a vertical integration criteria, pursuant to which ownership interests below 10% would not be attributable; ownership interests above 50% would be fully attributable; and ownership interests between 10% and 50% would be attributable on a prorated basis. TCI contends that this proposal embodies a clear, workable criteria that is superior to proposals favoring ad hoc disputes over the presence or absence of "control."[79]

60. E! Entertainment, ABC, BET, Turner and GTE, on the other hand,

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[76]See NCTA Comments at 18-19; Time Warner Comments at 31-32; Discovery Initial Comments at 19; CIC/CC Initial Comments at 38; Liberty Media Comments at 18-19; Viewer's Choice Comments at 5; IFE Initial Comments at 10.

[77]See Discovery Initial Comments at 19-20.

[78]See MPAA Comments at 7.

[79]See TCI Comments at 19-24.

support the Commission's proposal to use the Section 73.3555 broadcast attribution standards.[80] GTE argues that the Commission should establish a uniform attribution criteria in this dynamic period of convergence of communications technologies. Turner similarly maintains that the Commission should not apply a more restrictive attribution standard than currently applies to broadcasters.[81]

61. Discussion. Section 11(c)(2)(B) of the 1992 Cable Act does not indicate the appropriate criteria for determining vertical ownership attribution. The Senate Report, however, suggests that in determining what is an attributable interest, the Committee intended that the Commission use the attribution rules set forth in Section 73.3555 (Notes) of the Commission's rules or such other criteria as the Commission deems appropriate.[82] We conclude that the broadcast attribution criteria are appropriate for this purpose.

62. In the context of establishing limits on vertical integration in the cable industry we are concerned with identifying interests in cable programming services that are sufficient to afford influence or control over programming decisions. We also seek to identify interests that might potentially provide cable operators with an incentive to favor an affiliated video programming service over an unaffiliated or competing video programming service. However, we must balance these concerns with the objective of preserving the benefits and efficiencies of vertical integration and encouraging continued MSO investment in new video programming services. The broadcast attribution criteria are appropriate to address these competing concerns. The Section 73.3555 attribution criteria were designed to identify all interests that could potentially

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[80]See ABC Comments at 4; Turner Comments at 5-6; and GTE Comments at 3-5; BET Comments at 4-5; E! Entertainment Comments at 4-6. Alternatively, Rainbow Programming proposes a 10% attribution threshold, which it says will make no material difference in a cable operators ability to influence or control a video programmer. See Rainbow Comments at 5.

[81]See Turner Comments at 5.

[82]Senate Report at 80.

afford influence or control over management or programming decisions, while providing exceptions for interests above 5% if there is no realistic possibility of such interests imparting control. Thus, we conclude that the broadcast attribution criteria are strict enough to identify all interests that afford the potential to exert influence or control over management or programming decisions, yet flexible enough to permit continued MSO investment in new video programming services. Moreover, we believe that interests of 5% or greater may be substantial enough to motivate cable to systems to favor an affiliated programmer over a programmer in which the cable system has no attributable interest.

63. We decline to adopt a higher attribution threshold where more than one MSO holds a noncontrolling interest in a video programming service. Although we recognize that common ownership of a programming service by several MSOs may decrease the ability of any one MSO to assert influence or control over programming decisions, we nonetheless continue to believe that such minority interests may be sufficient to provide cable operators with an incentive to favor an affiliated video programming service over an unaffiliated service.

D. Percentage Limitation.

64. Further Notice. In the Further Notice we proposed a 40% limit on the number of channels that could be occupied by affiliated video programmers. Commenters were asked to indicate whether such a limit would be reasonable and would encourage MSOs to continue to invest in new video programming services. We noted that our intention was to establish a channel occupancy limit that would maximize the number of voices available to cable viewers without impairing the ability or incentive of cable operators to invest in new and existing video programming services.

65. Comments. NCTA and most cable commenters indicate that 40% is a minimally acceptable level at which to establish channel occupancy limits. Most cable commenters argue that the channel occupancy limits must be set high enough to preserve the benefits of vertical integration. In this regard, Discovery and Viacom suggest that a channel occupancy limit of 50% would be reasonable. Given the strict attribution standard

proposed by the Commission most cable commenters emphasize that it is essential that the Commission adopt a high enough channel occupancy limit to avoid impeding program investment and distribution. In addition, several commenters endorse the Commission's proposal to allow carriage of additional vertically integrated video programmers provided such video programmers are minority controlled.[83] These commenters agree that such an ownership incentive will increase minority ownership and promote program diversity.

66. TCI supports the proposed 40% limit but continues to advocate that rather than counting channels, the FCC should implement a system based on bandwidth. According to TCI, such an approach would be more precise and adaptable in the forthcoming era of digital compression. Under TCI's recommended approach, channel occupancy limits would be calculated by counting each 6 MHz segment as a single unit and applying limits on the number of units that could be occupied by vertically integrated programming. TCI submits that such an approach will encourage cable operators to continue to invest in the development of new technologies and innovative program services. TCI's proposal is supported by several other cable commenters.[84]

67. MPAA, NATOA and CFA, on the other hand, favor a 20% channel occupancy limit, stating that such a limit would reduce the risk of MSOs favoring affiliated programmers without inhibiting program investment. MPAA asserts that their proposed attribution threshold of 15% combined with a 20% channel occupancy limit better serves Congress' objectives of encouraging MSO investment in new video programming services, while increasing the channel capacity available to unaffiliated video programmers. MPAA suggests that the Commission's proposed 40% limit could result in many instances in no channels being available

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[83]See NATOA Comments at 10; BET Comments at 2-4; TCI Comments at 32; Turner Comments at 6; E! Entertainment Comments at 5; NCTA Comments at 22.

[84]See Time Warner Comments at 23-25; Turner Comments at 4; Liberty Media Initial Comments at 15-16.

to unaffiliated programmers.[85]

68. Discussion. We conclude that a 40% limit on the number of channels[86] that can be occupied by affiliated video programming services is reasonable to serve Congress' competing objectives in requiring such restrictions.[87] We believe that a 40% limit is appropriate to balance the goals of increasing diversity and reducing the incentive and ability of vertically integrated cable operators to favor their affiliated programming, with the benefits and efficiencies associated with vertical integration.[88] Congress and the Commission have both recognized that there

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[85]According to MPAA, it would be possible under the Commission's proposed 40% limit for a substantial number of 36 channel TCI systems to comply with the proposed rule while carrying no unaffiliated programming networks. MPAA adds that a 54 channel TCI system could comply with the proposed rule by "carrying as few as five unaffiliated programming networks." MPAA Comments at 7-8 (emphasis in original).

[86]We will measure the vertical ownership limits on a per channel basis, using the traditional 6MHz per channel definition. However, given the dynamic state of cable technology, we recognize that it may soon be common for cable operators to provide several channels using a single 6MHz bandwidth segment. Accordingly, as with our other rules we intend to review periodically this definition, and if necessary to make adjustments to ensure that it is consistent with the current state of technology.

[87]In order to calculate the exact number of channels on a vertically integrated cable system that can be devoted to carriage of programming in which the cable operator has an attributable interest parties should round up or down to the nearest decimal point. For example, on a system with 34-36 channels, 14 channels could be occupied by affiliated video programming services and on a system with 54-56 channels, 22 could be devoted to the carriage of affiliated programming services. In addition, where a single channel is shared by affiliated and unaffiliated video programming services, such channel will be counted as an affiliated channel only if the affiliated programming service accounts for 50% or more of the channel's programming time.

[88]We disagree with MPAA's assertion that a 40% limit could result in many instances in no channels being made available to unaffiliated video programmers. First, MPAA's calculation does not take into account the availability of leased access channels to unaffiliated video programmers. Second, MPAA appears to assume that TCI owned systems will drop popular unaffiliated programming services such as ESPN, USA Network and A & E in favor of other less popular affiliated programming services.

are benefits which result from vertical integration. First, MSO investment has produced a wealth of high quality cable programming services. Many of the most popular cable programming services were initiated or sustained with the help of MSO investment. Second, vertical integration between cable operators and video programming services appears to produce efficiencies in the distribution, marketing, and purchase of programming."[89] Third, vertical integration can reduce programming costs, which in turn may reduce subscriber fees and cable rates. Fourth, vertical integration may in certain circumstances foster investment in more innovative and riskier video programming services.

69. Moreover, Congress directed the Commission not to adopt limitations "which would impair the development of diverse and high quality video programming.[90] In this regard, we note that cable operators are already required to reserve a substantial percentage of their channel capacity for carriage of local broadcast and PEG stations.[91] In addition, cable operators are subject to leased access requirements, pursuant to which they may be required to designate an additional 15% of their activated channel capacity for commercial use by programmers unaffiliated with the cable operator.[92] Significantly, the leased access obligations are parallel in purpose to the channel occupancy requirements, since they also obligate cable operators to provide system access to

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The record evidence suggests that such conduct is fairly unlikely. See TCI Reply Comments at 13; Time Warner Reply Comments at 14. Finally, MPAA fails to acknowledge that cable systems carrying the maximum number of broadcast must carry and PEG stations are devoting substantial capacity to the carriage of unaffiliated programming.

[89]See Besen Study (attached to TCI Comments) at 23-24.

[90]47 U.S.C. § 533(f)(2)(G).

[91]Cable operators with more than 12 channels may be required to reserve 33% of their activated channel capacity for local broadcast and PEG channels. See 47 U.S.C. §§ 531, 534, 535.

[92]47 U.S.C. § 532.

unaffiliated video programmers. Thus, cable operators' ability to carry affiliated programming is already significantly curtailed by statutorily mandated carriage obligations.

70. We also note that channel occupancy limits are not the only means by which Congress intended to prevent anti-competitive conduct by vertically integrated MSOs. Sections 12 and 19 of the 1992 Cable Act establish specific behavioral restrictions prohibiting discrimination by vertically integrated cable operators and video programming services. As we indicated above, these provisions impose more narrowly tailored behavioral restraints, specifically prohibiting anti-competitive conduct by vertically integrated cable operators and programmers, while channel occupancy limits impose broader structural constraints, which affect the ability of all cable operators to carry programming in which they have an attributable interest. In addition, the must carry, leased access and PEG requirements imposed by other provisions of the Communications Act help to ensure that a diversity of views is available to cable subscribers. In light of the foregoing, we believe that the channel occupancy limits need not be unduly restrictive in order to prevent the incentive and the ability of cable operators to favor their affiliated programmers or to promote a diversity of views to cable subscribers.

71. In addition, in order to promote the presentation of a diversity of viewpoints on cable we will allow carriage of vertically integrated video programming services, on two additional channels or up to 45% of a cable system's channel capacity, which ever is greater, provided such additional video programming services are minority-controlled. As we indicated above with respect to horizontal ownership limits, the Commission has long recognized that the public interest is enhanced when cable programming reflects a diversity of viewpoints.[93] We believe that allowing such expanded carriage of minority-controlled video programming services will encourage additional MSO investment in minority-owned programming services, which will in turn promote minority

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[93]See para 28 supra, citing, Policy Statement on Minority Ownership of Cable Television Facilities, 52 RR2d 1469 (1982).

ownership of video programming services and increase the diversity of viewpoints presented to cable subscribers. In this regard, we believe that the diversity benefits of such increased minority ownership outweigh the access concerns associated with such an increase in integration. We decline, however, to adopt a similar policy for minority oriented- programming. Although we seek to encourage the presentation of a diversity of viewpoints on cable television including those of minorities, we believe that increasing minority ownership of cable systems and video programming services is the most effective and legally sound means of promoting such diversity.[94]

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[94]See Metro Broadcasting v. FCC, 110 SCt. 2997, 3019 and n. 36 (1990) (noting substantial practical and constitutional difficulties that would be presented by FCC promotion of broadcast program diversity through direct program regulation rather than through structural means such as ownership).

G. Effective Competition.

85. Further Notice. In the Further Notice we observed that once effective competition has been established and a cable operator no longer occupies a program access bottleneck position, channel occupancy limits may no longer be necessary or desirable. Thus, we proposed to phase out channel occupancy limits in communities where effectivecompetition is established. We asked commenters to indicate whether the definition of effective competition for this purpose should include cable systems subscribed to by fewer than 30% of the homes located in the franchise area.

86. Comments. Cable commenters addressing this issue all favored our proposal to phase out channel occupancy restrictions in communities where effective competition has developed.[108] Where effective competition exists, these commenters assert that non-vertically integrated video programmers clearly have alternative outlets for programming. In addition, these commenters indicate that there is no incentive for cable operators to favor their affiliated video programming services over unaffiliated or competing video programming services in a competitive marketplace. According to one cable commenter, maintaining such limits where effective competition is established might hinder competition, by enabling a multichannel video program distributor to carry programming owned by a cable operator that the cable operator would not be permitted to carry.

87. MPAA and NATOA, on the other hand, oppose eliminating channel occupancy limits in communities where effective competition develops. MPAA observes that a competing multichannel distributor may also be vertically integrated and removing channel caps in these instances would result in foreclosure of nonaffiliated programmers from either outlet. Both MPAA and NATOA contend that the effective competition standard relates only to rate regulation and is not relevant to the ability of a vertically integrated cable operator to preclude a

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[108] See NCTA Comments at 24; Liberty Media Comments at 16; Time Warner Comments at 37; TCI Initial Comments at 39; Viacom Initial Comments at 17-18; Turner Comments at 7; Discovery Comments at 5-7.

video programmer from obtaining access to subscribers.

88. Discussion. We conclude that we should not eliminate channel occupancy limits in communities where effective competition exists. Although it is argued that the development of effective competition will preclude cable operators from exercising undue power in these situations, the effective competition standard was not adopted for this specific purpose and it is not clear that the presence of effective competition for any cable system addresses all of the relevant concerns that Congress expressed in enacting Section 11 of the Act. For example, if a programming service is excluded from carriage on a competitive system for reasons related to vertical integration, that service will continue to be disadvantaged, and the diversity and competition objectives of this portion of the Cable Act will be frustrated. Thus, at this time, we are not prepared to say that the presence of "effective competition" is a reasonable basis for removing the channel occupancy caps.

89. Congress has, however, indicated that a primary objective of the Act was to "rely on the marketplace to the maximum extent feasible, to promote the availability to the public of a diversity of views and information" and that the legislation was intended to protect consumer interests in the receipt of cable service "where cable television systems are not subject to effective competition.[109] Thus, as with a number of other aspects of these rules, further analysis as to whether the restrictions might be phased out where effective competition develops will be appropriate as we gain more experience with the rules.

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[109] 1992 Cable Act, Section 2(b).

C. Ordering Clauses.

109. Accordingly, IT IS ORDERED that pursuant to the authority contained Sections 2(a), 4(i) and (j) and 303 of the Communications Act of 1934, as amended, and the Cable Television Protection and Competition Act of 1992, Pub.L. No. 102-385, Part 76 of the Commission's Rules, 47 C.F.R. Part 76, Is AMENDED as set forth in Appendix D below, and will become effective January 10, 1994, subject to approval by the Office of Management and Budget. However, the effective date of the horizontal ownership limits contained in Section 76.503 of the Commission's rules IS STAYED pending final judicial resolution of the District Court decision in Daniels Cablevision v. United States, No. 92- 2292 (D.D.C. released September 16, 1993) holding such rules unconstitutional.

E. Additional Information.

110. For additional information regarding this proceeding, contact Jacqueline Chorney, Mass Media Bureau, (202) 632-6990.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton

Appendix D

Rule Changes

Part 76 of Title 47 of the Code of Federal Regulations is amended to read as follows:

76--CABLE TELEVISION SERVICE

1. The authority citation for Part 76 continues to read as follows:

Authority: Secs. 2, 3, 4, 301, 303, 307, 308, 309, 48 Stat., as amended, 1064, 1065, 1066, 1081, 1082, 1083, 1084, 1085, 1101; 47 U.S.C. Secs. 152, 153, 154, 301, 303, 307, 308, 309, 532, 533, 535, 542, 543, 552, as amended 106 Stat. 1460.

2. Part 76 is amended by adding Section 76.503 to read as follows:

§ 76.503 National Subscriber Limits

* * * * *

(a) Except as set forth in paragraph (b) of this section no person or entity shall be permitted to reach more than 30% of all homes passed nationwide through cable systems owned by such person or entity or in which such person or entity holds an attributable interest.

(b) Ownership of cable systems reaching up to 35% of all homes passed nationwide shall be permitted provided the additional cable systems, beyond 30% of homes passed nationwide, are minority-controlled.

(c) Prior to acquiring additional cable systems any person or entity holding an attributable interest in cable systems reaching 20%, or more, of homes passed nationwide must certify to the Commission that no violation of the national subscriber limits prescribed in this section will occur as a result of such acquisition.

Note 1: For purposes of this Section:

(a) "Minority-Controlled" means more than 50% owned by one or more members of a minority group.

(b) "Minority" means Black, Hispanic, American Indian, Alaska ative, Asian and Pacific Islander.

(c) "Attributable Interest" shall be defined by reference to the criteria set forth in the Notes to § 76.501.

* * * * *

3. Part 76 is amended by adding Section 76.504 to read as follows:

§ 76.504 Limits on Carriage of Vertically Integrated Programming

(a) Except as otherwise provided in this section no cable operator shall devote more than 40% of its activated channels to the carriage of national video programming services owned by the cable operator or in which the cable operator has an attributable interest.

(b) The channel occupancy limits set forth in paragraph (a) shall apply only to channel capacity up to 75 channels.

(c) A cable operator may devote two additional channels or up to 45% of its channel capacity, whichever is greater, to the carriage of video programming services owned by the cable operator or in which the cable operator has an attributable interest provided such video programming services are minority- controlled.

(d) Cable operators carrying video programming services owned by the cable operator or in which the cable operator holds an attributable interest in excess of limits set forth in paragraph (a) as of December 4, 1992 shall not be precluded by the restrictions in this section.

(e) Cable operators are required to maintain records in their public file for a period of three years regarding the nature and extent of their attributable interests in all video programming services as well as information regarding their carriage of such verticlaly integrated video programming services on cable systems in which they also have an attributable interest. These records must be made available to local franchise authorities, the Commission, or members of the public on reasonable notice and during regular business hours.

Note 1: For purposes of this Section:

(a) "Minority-Controlled" means more than 50% owned by one or more members of a minority group.

(b) "Minority" means Black, Hispanic, American Indian, Alaska Native, Asian and Pacific Islander.

(c) "Attributable Interest" shall be defined by reference to the criteria set forth in the Notes to § 76.501.

* * * * *

App. 95

SEPARATE STATEMENT OF
COMMISSIONER ANDREW C. BARRETT

RE: Implementation of the Cable Television Consumer Protection and Competition Act of 1992--Cable Ownership

This Second Report and Order adopts regulations regarding horizontal ownership and channel occupancy limits. In particular, the Commission establishes (1) a horizontal limit at 30% of homes passed nationally by cable systems owned by any single entity, with an allowance for ownership of systems totalling an additional 5% beyond the horizontal limit provided that such systems are minority controlled; and (2) a 40%-limit for channels occupied by programming services that are vertically integrated with a particular cable operator, applicable up to 75 channels. Regarding the channel occupancy limit, the rules allow for an additional two channels, or 5% of the cable system's total channels, whichever is greater, provided that the services are minority controlled.

I write separately to emphasize the importance of the horizontal and vertical ownership limits as structural measures addressing the aspects of concentration and vertical integration in the multichannel marketplace. In particular, I am concerned that these measures must be viewed the context of the Commission's prior decisions on rate regulation and program access, as well as the rules adopted today concerning program carriage agreements.[110] Given the existing behavioral regulations imposed on vertically integrated cable operators and programming vendors, these cable ownership provisions will become the

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[110] See Rate Order and Further Notice of Proposed Rule Making, MM Docket No. 92-266, FCC 93-177, released May 3, 1993; 58 Fed.Reg. 29736. See also First Report and Order, MM Docket No. 92-265, 8 FCCRcd 3359 (1993); Second Report and Order, MM Docket No. 92-265, adopted September 23, 1993.

structural component that will govern the cable industry's transition from a regulated environment to effective competition. In this regard, I believe that greater availability of programming services to all distributors will play a critical role in determining whether the future broadband network will ultimately belong to all multichannel competitors, including cable operators, to the extent that they remain able to invest and exercise creativity. Therefore, I am concerned that the channel occupancy rules must incorporate sufficient flexibility to permit future opportunities for investment leading to the development of new ventures and programming.

I am also interested in the higher thresholds established to allow for ownership and channel occupancy where cable systems and programming services are minority controlled. I support these provisions that will promote opportunities for greater participation by minority enterprises in the multichannel marketplace as program vendors and distributors.

Finally, the horizontal ownership provisions are affected by the decision by the United States District court for the District of Columbia regarding the constitutionality of this portion of Section 11 of the 1992 Cable Act.[111] Although the Court has found the statute's numerical limit on subscribers unconstitutional, the decision includes a provision to stay the results pending completion of any proceedings on appeal. Therefore, I am concerned that the Commission will need to monitor the development of this litigation and the ramifications of any further events concerning the effectiveness of the cable ownership rules, especially to the extent that any developments regarding the vertical limits could affect the availability of programming services.

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[111]See Daniels Cablevision v. United States of America, No. 92-2292 [D.D.C., released September 16, 1993].

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Cable	)	
Television Consumer Protection	)	CS Docket No. 98-82
and Competition Act of 1992	)	
	)	
Review of the Commission's	)	
Cable Attribution Rules	)	

NOTICE OF PROPOSED RULEMAKING

Adopted: June 4, 1998 Released: June 26, 1998

Comment Date: August 14, 1998

Reply Comment Date: September 3, 1998

By the Commission:

I. INTRODUCTION

1. With this *Notice of Proposed Rulemaking*, we initiate a review of our cable attribution rules, which define what constitutes a "cognizable interest" that triggers application of various Commission rules relating to the provision of cable television services. The attribution rules seek to identify those corporate, financial, partnership, ownership and other business relationships that confer on their holders a degree of ownership or other economic interest, *or* influence or control over an entity engaged in the provision of communications services such that the holders should be subject to the Commission's regulation. We are initiating this rulemaking in light of recent developments in the cable industry, including numerous strategic alliances, partnerships, system swaps, mergers and acquisitions among cable entities; various Commission proceedings related to the issue of cable ownership, such as the cross-ownership proceedings, horizontal ownership proceedings, and biennual review; and the Commission's review, in a separate proceeding, of the broadcast attribution rules on which many of our

cable attribution rules were based.[1] Where appropriate, we provide a brief summary of the attribution issues contained in the *Broadcast Attribution Notice* and *Broadcast Attribution Further Notice*; for a full discussion of these issues, interested parties are directed to review those documents.

II. NOTICE OF PROPOSED RULEMAKING

2. *Background.* The cable attribution rules are particularly significant in the context of a number of statutory provisions enacted as part of the Cable Television Consumer Protection and Competition Act of 1992[2] (the "1992 Cable Act"), including: (1) former Section 613(a)(1), which prohibited the common ownership of local television stations and cable systems that serve the same area (the "cable/broadcast station cross-ownership restriction");[3] (2) Section

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[1] *See Notice of Proposed Rule Making, Review of the Commission's Regulations Governing the Attribution of Mass Media Interests*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 94-324, 10 FCC Rcd 3606 (1995) ("*Broadcast Attribution Notice*"); *Further Notice of Proposed Rule Making, Regulations Governing Attribution of Broadcast and Cable/MDS Interests, Regulation and Policies Affecting Investment in the Broadcast Industry and Reexamination of the Commission's Cross-Interest Policy*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 96-436, 11 FCC Rcd 19895 (1996) ("*Broadcast Attribution Further Notice*").

[2] Pub. L. No. 102-385, 106 Stat. 1460 (1992), 47 U.S.C. § 521, *et seq.* (1992).

[3] Section 613(a)(1) of the Communications Act of 1934, as amended (the "Communications Act"), 47 U.S.C. § 533(a)(1) (1992). The cable/broadcast station cross-ownership rule was first adopted by the Commission in 1970 and modified in 1992. *See Second Report and Order, Amendment of Part 74, Subpart K, of the Commission's Rules and Regulations Relative to Community Antenna Television Systems; and Inquiry into the Development of Communications Technology and Services to Formulate Regulatory Policy and Rulemaking and/or Legislative Proposals*, Docket No. 18397, 23 FCC 2d 816 (1970); *Report and Order, Amendment of Part 76, Subpart J, Section 76.501 of the Commission's Rules and Regulations to Eliminate The Prohibition on Common Ownership of Cable Television Systems and National Television Networks*, MM Docket No. 82-434, 7 FCC Rcd 6156, 6174 n.54 (1992); 47 C.F.R. § 76.501. The cable/broadcast station cross-ownership restriction was codified by statute in the Cable Communications Policy Act of 1984, Pub. L. No. 98-549, 98 Stat. 2779 (1984). Although the Telecommunications Act of 1996 eliminated the statutory cable/broadcast station cross-ownership restriction, it left in place the

613(f)(1)(A), which requires the Commission to establish reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest ("horizontal cable ownership limits");[4] (3) Section 613(f)(1)(B), which requires the Commission to establish reasonable limits on the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest ("vertical occupancy limits");[5] (4) Section 613(a)(2), which prohibits a cable operator from holding a license to provide multichannel multipoint distribution service ("MMDS"), or from offering satellite master antennae television ("SMATV") service separate and apart from any franchised cable service, in any portion of the franchise area served by the cable operator's cable system (the "cable/MMDS" and "cable/SMATV" cross-ownership restrictions);[6] (5) Section 628, which, among other things, requires the Commission to

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Commission's equivalent rule at 76 C.F.R. § 76.501, pending Commission review of our rules. *See* Section 202(i)(1) of the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (the "1996 Act"); *Joint Explanatory Statement of the Committee of Conference, Telecommunications Act of 1996*, S. Rep. 104-230 at 164 (February 1, 1996) ("The conferees do not intend that this repeal of the statutory prohibition should prejudge the outcome of any review by the Commission of its rules.") The 1996 Act also eliminated the prohibition on broadcast television networks' ownership or control of cable systems, and the Commission has amended our rule at 76 C.F.R. § 76.501 to eliminate the prohibition in conformity therewith. *See* 1996 Act, Section 202(f); *Order Implementing Sections 202(f), 202(i) and 301(i) of the Telecommunications Act of 1996*, CS Docket No. 95-56, FCC 96-112, 11 FCC Rcd 15115 (1996).

[4] Communications Act § 613(f)(1)(A), 47 U.S.C. § 533(f)(1)(A).

[5] Communications Act § 613(f)(1)(B), 47 U.S.C. § 533(f)(1)(B).

[6] Communications Act § 613(a)(2), 47 U.S.C. § 533(a)(2) (now Communications Act § 613(a), 47 U.S.C. § 533(a)). The 1996 Act amends this provision to state that it does not apply to any cable operator in any franchise area in which that cable operator faces "effective competition." *See* 1996 Act § 202(i)(6), codified at Communications Act § 613(a)(3), 47 U.S.C. § 533(a)(3), and the Commission's rules implementing this provision
at 47 C.F.R. §§ 21.912(e)(3), 76.501(f).

establish safeguards to prevent a cable operator with an attributable interest in a programming vendor from engaging in unfair or deceptive acts involving the distribution of programming to an unaffiliated multichannel video programming distributor ("program access" rules);[7] and (6) Section 616, which, among other things, restricts the activities of cable operators and other multichannel programming distributors when dealing with programming vendors, including prohibiting discrimination in the selection, terms, or conditions of carriage, on the basis of a vendor's affiliation or non-affiliation ("program carriage" rules).[8] Implementation of the foregoing rules serve two goals: (1) promoting diversity; and (2) deterring anticompetitive practices. As discussed below, for those cable ownership rules implemented to promote competition and diversity, the Commission adopted attribution rules from the broadcast context where the goal is the same. For those rules implemented to deter specific improper practices as well as to promote competition and diversity, the Commission adopted stricter attribution standards.

3. In 1984, the Commission conducted a comprehensive rulemaking proceeding and decided to adopt a single attribution standard for our cross-ownership rules which govern the extent to which a single entity may simultaneously hold ownership interests in

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[7] Communications Act § 628(b), 47 U.S.C. § 548(b). *See also First Report and Order, Implementation of Sections 12 & 19 of the Cable Television Consumer Protection and Competition Act of 1992 -- Development of Competition and Diversity in Video Programming and Distribution and Carriage*, MM Docket 92-265, 8 FCC Rcd 3359, 3370 (1993) ("*Program Access Order*"), *recon. granted in part, Memorandum Opinion and Order on Reconsideration of the First Report and Order*, MM Docket No. 92-265, 10 FCC Rcd 1902 (1994) ("*Mem. Op. on Recon. of Program Access Order*").

[8] Communications Act § 616(a), 47 U.S.C. § 536(a). *See also Second Report and Order, Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992 -- Development of Video Programming Distribution and Carriage*, MM Docket No. 92-265, 9 FCC Rcd 2642, 2643-44 (1993) ("*Program Carriage Order*").

broadcast stations, cable television systems, and newspaper entities.[9] Although we did not perform a separate analysis of the ownership structures of cable systems, we were "reasonably certain" that they were not sufficiently different from broadcasting to justify the adoption of a distinct benchmark.[10] The resulting standard (the "broadcast attribution standard") generally provides that partnership interests, direct ownership interests, and voting stock interests of 5% or more are attributable. For passive investors, the voting stock benchmark is 10%. Non-voting stock interests (including most "preferred" stock classes) are not attributable. There are several exceptions to the voting stock threshold, including a "single majority shareholder" exception, which provides that minority interests will not be attributed where a single shareholder owns more than 50% of the outstanding voting stock. In addition, the interests of "insulated" limited partners are not attributed.[11]

4. In our rulemaking proceedings under the 1992 Cable Act, we determined that the broadcast attribution standard still governs broad structural rules, such as the horizontal cable ownership limits[12] and vertical channel occupancy limits,[13] that are designed to

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9 *See Report and Order, Amendment of the Rules concerning Attribution of Ownership of Broadcast Licensees,* MM Docket No. 83-46, 97 FCC 2d 997, 1032 (1984), *recon. in part, Memorandum Opinion and Order,* MM Docket No. 83-46, FCC 85-252, 58 RR 2d 604 (rel. June 24, 1985), *further recon. granted in part, Memorandum Opinion and Order,* MM Docket No. 83-46, FCC 86-410, 1 FCC Rcd 802 (1986).

10 *Id.* at 1033 n.85.

11 *See* 47 C.F.R. § 73.3555 n.2 (an "insulated" limited partner is one certified as having "no material involvement, directly or indirectly, in the management or operation of the media activities of the partnership").

12 *See Second Report and Order, Implementation of Sections 11 & 13 of Cable Television Consumer Protection and Competition Act of 1992 -- Horizontal and Vertical Ownership Limits,* MM Docket No. 92-264, 8 FCC Rcd 8565, 8568-69, 8577-8579 (1993) ("*Horizontal/Vertical Ownership Order*"). In the *Horizontal/Vertical Ownership Order,* the Commission voluntarily stayed the effective date of the horizontal ownership rules pending final judicial resolution of the District Court decision in *Daniels Cablevision, Inc. v.*

ensure competition and diversity in the video marketplace. In adopting the broadcast attribution standard for our rules restricting horizontal and vertical ownership, we also were guided by the legislative history of the 1992 Cable Act, which expressly suggested use of the broadcast attribution standard, and which directed that, along with the dangers of increased concentration, we should also consider the potential benefits of increased concentration -- e.g., increased economies of scale and increased capital investment in cable programming.[14] In light of these considerations, we found that a more restrictive attribution standard than the broadcast standard was not warranted for application to the structural rules.

5. We have adopted a more restrictive attribution standard, however, for those rules designed not only to promote competition and diversity, but also to deter specific discriminatory or improper conduct by cable operators or programmers. In contrast to the broadcast attribution standard, this more restrictive standard (1) considers a cable operator to have an attributable interest if it holds 5% or more of an entity's stock, whether voting or non-voting, (2) does not apply the single majority shareholder rule, and (3) attributes limited partnership interests of 5% or more, regardless of insulation.

6. We have adopted the more restrictive standard for our

United States, 835 F. Supp. 1, 10 (D.D.C. 1993), *aff'd in part, Time Warner Entertainment Co., L.P. v. FCC*, 93 F.3d 957 (D.C. Cir. 1996), which held that the underlying statute violates the First Amendment. *Horizontal/Vertical Ownership Order* at ¶ 3. In August 1996, the D.C. Circuit Court consolidated the *Daniels* appeal and *Time Warner Entertainment Co., L.P. v. FCC*, No. 94-1035 (D.C. Cir. 1994), a challenge to the Commission's rules. *Time Warner Entertainment Co., L. P. v. FCC*, 93 F.3d 957, 979-80 (D.C. Cir. 1996). The D.C. Circuit determined to hold court proceedings in abeyance while the Commission reconsidered the horizontal ownership rules. *Id.*

13 *Horizontal/Vertical Ownership Order*, 8 FCC Rcd at 8593-8596.

14 *See Report of the Senate Committee on Commerce, Science and Transportation*, S. Rep. No. 92, 102d Cong., 1st Sess. 80 (1991). Congress' intent is reflected in the 1992 Cable Act § 11(f)(2), 47 U.S.C. § 533(f)(2), which requires the Commission to weigh both the dangers and the benefits of increased concentration in promulgating our rules.

rules imposing specific behavioral restraints on cable operators and programmers, such as our rules regarding program access and program carriage, both of which were designed, in part, to prevent cable operators from using their market power to engage in improper conduct.[15] In our program access rulemaking, we noted that the more restrictive standard was being adopted in light of Congress' purpose in adopting Section 628: curbing certain incentives to influence the behavior of affiliates to the detriment of competitors.[16] While we acknowledged that one of the rule's objectives was to promote general competition and diversity in the video marketplace, the additional anti-discrimination objective warranted "a relatively inclusive attribution rule."[17] Similarly, in the MMDS and SMATV cross-ownership context, we adopted the more restrictive attribution standard in order to prevent cable operators from "warehousing potential competition," as well as to encourage the development of competition to established cable operators by alternative multichannel video service providers.[18]

7. In addition, we have relied upon our attribution rules in defining when an entity is considered an "affiliate" for certain purposes under Title VI. For instance, we have applied the more restrictive attribution standard to the ratemaking context, for purposes

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15 *See Program Access Order*, 8 FCC Rcd at 3370-71; *Program Carriage Order*, 9 FCC Rcd at 2650. *See also* 47 C.F.R. §§ 76.1000(b), 76.1300(a).

16 *See Program Access Order*, 8 FCC Rcd at 3370-71, *citing Second Report and Order, Recommendation to Congress, and Second Further Notice of Proposed Rulemaking, Telephone Company-Cable Television Cross-Ownership Rules, Section 63.54 - 63.58*, CC Docket No. 87-266, 7 FCC Rcd 5781 (1992); *see also Mem. Op. on Recon. of Program Access Order*, 10 FCC Rcd 1902, 1911-27 (rejecting various proposed exemptions from 5% attribution standard).

17 *Program Access Order*, 8 FCC Rcd at 3360, 3370. *See* 47 C.F.R. § 76.1000(b).

18 *See Report and Order and Further Notice of Proposed Rulemaking, Implementation of Sections 11 & 13 of Cable Television Consumer Protection and Competition Act of 1992 -- Cross-Ownership Limitations and Antitrafficking Provisions*, MM Docket No. 92-264, 8 FCC Rcd 6828, 6843-46 (1993); *see also* 47 C.F.R. §§ 21.912 n.1, 76.501(d)-(e).

of analyzing asset transfers and the provision of services between a cable operator and its affiliate.[19] We found that, in enacting the 1992 Cable Act, Congress intended to ensure that consumers pay reasonable rates for regulated cable services, and that it would be inconsistent with Congress' intent to allow cable operators to impose the costs of nonregulated activities on regulated cable services through improper cross-subsidization.[20] To deter such conduct, we held that the more restrictive attribution rule should apply. We also applied the more restrictive attribution standard to our rules limiting the amount of pass-throughs permitted for programming services affiliated with cable multiple system operators.[21] Those rules arose out of a concern about abuses that might occur if a vertically integrated cable operator were permitted to engage in unlimited pass-throughs to subscribers of the cost of programming that the operator obtained from an affiliated entity.[22]

8. Similarly, in adopting a definition of "affiliate" for purposes of the leased access provisions[23] and the open video system provisions,[24] we adopted the more restrictive attribution standard.[25]

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19 *See Report and Order and Further Notice of Proposed Rulemaking, Implementation of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation and Adoption of a Uniform Accounting System for Provision of Regulated Cable Services,* MM Docket No. 93-215, 9 FCC Rcd 4527, 4663-68 (1994). *See also* 47 C.F.R. § 76.924(i).

20 *Id.* at 4663-64.

21 *See Report and Order and Further Notice of Proposed Rulemaking, Implementation of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation,* MM Docket No. 92-266, 8 FCC Rcd 5631, 5787-88 (1993), *citing* 47 C.F.R. § 76.1000(b).

22 *Id.*

23 Communications Act § 612, 47 U.S.C. § 532.

24 Communications Act § 653, 47 U.S.C. § 573.

25 *See* 47 C.F.R. §§ 76.970(b), 76.1500(g); *Second Report and Order and Second Order on Reconsideration of the First Report and Order, Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 -- Leased Commercial Access,*

We found that, in addition to promoting diversity, these provisions were designed to reduce the likelihood that cable operators and open video system operators will discriminate against or otherwise disfavor unaffiliated programming providers.[26] Given these dual objectives, we found that the more restrictive attribution standard was the appropriate standard for identifying the interests at issue.[27]

9. Finally, we note that in the "Cable Act Reform" proceeding[28] we are reviewing appropriate definitions of "affiliate" under other provisions of the 1996 Act, including the small operator provisions,[29] the new prong of the "effective competition" test,[30] and the cable-telco buy-out provisions.[31] Pending the adoption of final rules, we requested comments on the appropriate definition of "affiliate" for the cable-telco buyout provisions[32] and established interim rules for the small operator and "effective competition" provisions. For the small operator provisions, the interim rule adopted the definition of "affiliate" used for purposes of our small system cost-of-service rules.[33] Thus,

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CS Docket No. 96-60, FCC 97-27, 12 FCC Rcd 5267 (1997), at paras. 118-121 ("*Leased Access Order*"); *Third Report and Order and Second Order on Reconsideration, Implementation of Section 302 of the Telecommunications Act of 1995; Open Video Systems*, CS Docket No. 96-46, FCC 96-334, 11 FCC Rcd 20227 (1996), at paras. 4-16 ("*OVS Order*").

26 *OVS Order* at para. 14; *Leased Access Order* at para. 119.

27 *OVS Order* at paras. 14-15; *Leased Access Order* at para. 119.

28 *See Order and Notice of Proposed Rulemaking, Implementation of Cable Act Reform Provisions of the Telecommunications Act of 1996*, CS Docket No. 96-85, FCC 96-154, 11 FCC Rcd 5937 (1996) ("*Cable Act Reform NPRM*").

29 *See* Communications Act § 623(m)(2), 47 U.S.C. § 543(m)(2).

30 *See* Communications Act § 623(l)(1)(D), 47 U.S.C. § 543(l)(1)(D).

31 *See* Communications Act § 652, 47 U.S.C. § 572.

32 *Cable Act Reform NPRM* at ¶ 96.

33 *Cable Act Reform NPRM*, 11 FCC Rcd at 5947-48, *citing* 47 C.F.R. § 76.934(a). *See also Sixth Report and Order and Eleventh Order on Reconsideration, Implementation of*

an entity is deemed affiliated with a small cable operator if that entity has a 20% or greater equity interest in the operator (active or passive) or holds de jure or de facto control over the operator.[34] By contrast, in the "effective competition" context, the Commission found it reasonable to adopt an interim rule that reflected the new Title I affiliation threshold that Congress has prescribed for other provisions of the Communications Act.[35] Under the new standard, an affiliate is an entity that (directly or indirectly) owns or controls, is owned or controlled by, or is under common ownership or control with, another person, where the term "own" means to have an equity interest (or the equivalent thereof) of more than 10%.[36]

10. *Notice.* As noted above, we released the *Broadcast Attribution Notice* and the *Broadcast Attribution Further Notice* to review our broadcast attribution standard. Among the issues on which we solicited comment in the *Broadcast Attribution Notice* were: (1) whether to increase the voting stock ownership benchmark from 5 percent to 10 percent;[37] (2) whether to increase the passive investor stock ownership benchmark from 10 percent to 20 percent;[38] (3) whether to restrict or eliminate our single majority shareholder exemption and whether to attribute nonvoting shares in certain circumstances, such as where the minority or nonvoting shareholder has contributed a significant

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Section of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket Nos. 92-266 & 93-215, FCC 95-196, 10 FCC Rcd 7393 (1995).

34 *See Cable Act Reform NPRM,* 11 FCC Rcd at 5947-48.

35 *Id.* at 5943-44.

36 *See* Communications Act § 3(1), 47 U.S.C. § 153(1); *see also* 47 C.F.R. § 76.1401(b).

37 *Broadcast Attribution Notice* at paras. 18-46.

38 *Id.* at paras. 47-50. We also invited comment on our tentative conclusion not to expand the passive investor class to include pension funds, investment and commercial banks, and certain investment advisors.

portion of the equity or debt financing;[39] (4) whether to revise our insulation criteria for limited partnership interests, and whether to adopt an equity benchmark for noninsulated limited partners;[40] (5) whether to treat interests in limited liability companies ("LLCs") and similar new business forms, such as registered limited liability partnerships ("RLLPs"), as we now treat limited partnerships;[41] (6) whether to eliminate the remaining aspects of our cross-interest policy that prevent individuals from having "meaningful" interests -- including key employee relationships, joint ventures, and nonattributable equity interests -- in two broadcast stations, or a daily newspaper and a broadcast station, or a television station and a cable system, when both outlets serve "substantially the same area;"[42] and (7) how to treat non-equity financial relationships and multiple business relationships that, although not individually attributable, could combine to create sufficient influence to warrant attribution.[43]

11. In addition to the issues raised in the *Broadcast Attribution Notice*, the *Broadcast Attribution Further Notice* explored additional proposals to increase the precision of the attribution rules. First, we invited comment on whether we should add a new "equity or debt plus" ("EDP") attribution rule. Under such a rule, where an interest holder is a program supplier or same-market media entity, we will attribute its otherwise non-attributable equity and/or debt interests in a licensee or other media entity subject to the cross-ownership rules if those aggregated interests exceed a specified benchmark, proposed to be set at 33 percent.[44] Second, we tentatively concluded that we should

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39 *Id.* at paras. 51-54.

40 *Id.* at paras. 55-63.

41 *Id.* at paras. at 64-75.

42 *Id.* at paras. 76-92.

43 *Id.* at paras. 93-100.

44 *Broadcast Attribution Further Notice* at paras. 8-25.

treat television time brokerage agreements or local marketing agreements ("LMAs") the same as radio LMAs, and also count radio and television LMAs toward all applicable ownership limits.[45] Third, we invited comment as to whether we should attribute joint sales agreements ("JSAs") in certain circumstances.[46] Fourth, we invited comments on a Commission staff study of attributable ownership interests in broadcast television stations, appended to the *Broadcast Attribution Further Notice*, and on the implications of this study regarding the impact of the proposed attribution rule changes, particularly as to the voting stock benchmarks.[47] Fifth, we sought comments on whether a transition period or grandfathering of existing interests is appropriate. We tentatively concluded that any grandfathering should apply only to the current interest holder and that interests acquired on or after December 15, 1994, the date of adoption of the *Broadcast Attribution Notice*, should be subject to any final rules adopted.[48] Finally, we invited comments as to whether we should apply broadcast attribution criteria and add a new EDP attribution rule for purposes of the cable/Multipoint Distribution Service ("MDS") cross-ownership restrictions.[49]

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[45] *Id.* at paras. 26-31. For purposes of applying the radio LMA rules, the Commission's rules define time brokerage as "the sale by a licensee of discrete blocks of time to a 'broker' that supplies the programming to fill that time and sells the commercial spot announcements in it." 47 C.F.R. § 73.3555(a)(4)(iii). The *Broadcast Attribution Further Notice* refers to LMAs as "those time brokerage agreements involving a broker that is a licensee of one or more stations in the same market as the brokered station." *Id.* at para. 2 n. 4.

[46] *Id.* at paras. 32-35. JSAs are agreements between broadcasters for the joint sales of broadcast commercial time. *Id.* at para. 33.

[47] *Id.* at paras. 36-38 and Commission staff study attached thereto.

[48] *Id.* at paras. 39-42. We reiterated that the issue of grandfathering of television LMAs would be addressed separately in the television local ownership proceeding. *Id.* at para. 40.

[49] *Id.* at paras. 43-44.

12. This *Notice* initiates a similar review of attribution issues as they specifically relate to our cable rules.[50] We note that the ownership attribution rules are intended to identify those relationships that confer on their holders a degree of influence or control over key business decisions, including budget, personnel, programming, and technology practices of cable entities, such that the holders should be subject to the Commission's regulations. In addition, the attribution rules may be used to identify ownership or other relationships that could provide the entities involved with economic incentives to operate in conflict with the objectives of the particular cable regulation at issue. We seek comment on the same issues raised in the broadcast attribution proceedings as they pertain to the cable industry, and on whether and how these issues should factor into the review of our cable attribution rules. In particular, we ask commenters to focus on: (1) the proposed "equity or debt plus" addition to the current attribution rules, and specifically those relationships in the cable context that may provide sufficient incentive and ability for an otherwise nonattributable interest holder to exert an attributable influence or control; (2) the attribution of certain contractual or other business relationships in the cable context (including affiliations that allow different cable entities to purchase programming, technology or equipment on common terms, analogous to JSAs and LMAs in the broadcast context) that may implicate diversity and competition concerns, irrespective of debt or equity; (3) the impact of raising the stock ownership benchmark for active and passive investors in the cable context, particularly seeking empirical data and analysis similar to the Commission staff study on the same subject in the broadcasting context; (4) whether to retain, modify, or eliminate the single majority shareholder exemption; and

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[50] We have received informal communications suggesting such a comprehensive review of our attribution rules. *See, e.g.*, Letter from S. White Rhyne and Robert L. Petit of the Federal Communications Bar Association to Reed E. Hundt, dated January 30, 1995 (urging the Commission, as part of "reinventing government" efforts, to initiate a comprehensive review of the attribution tests used by its various bureaus and offices in order to promote consistency of interpretation and process).

(5) whether a transition period or grandfathering of existing interests is appropriate if we decide to adopt more restrictive attribution rules. Because the *Broadcast Attribution Notice* and the *Broadcast Attribution Further Notice* already address application of the attribution rules to the cable/MMDS and the cable/broadcast cross-ownership restrictions, we will not revisit and therefore do not seek comment on those issues in this proceeding.[51]

13. We seek comment on whether the assumptions underlying our cable attribution rules are still valid. In particular, we solicit comment on whether any relevant differences exist between the cable and broadcasting industries that would support a distinct cable attribution standard even for those cable rules designed, like our broadcasting ownership rules, to ensure competition and diversity. We note that the broadcast attribution rules focus primarily on those relationships which confer on their holders influence or control over a broadcaster's key business decisions in the areas of budget, personnel and programming. We seek comment on whether, in the cable context, these are the appropriate key business areas and whether the underlying areas of concern should include cable entities' technology decisions and practices. We seek comment on whether there are differences in ownership, financing or management structures, industry health, typical stockholdings, informal business arrangements, or outside financial claims that render one of the industries more or less subject to the types of influence or control that our attribution rules seek to identify. Also, because our current cable attribution rules do not distinguish between types of cable operators, we seek comment on whether any relevant differences exist among cable operators that would warrant different attribution rules.

14. We also solicit comment on whether and how we should re-evaluate the more restrictive attribution standard applicable to certain of the rules described above, such as the program access and program carriage rules and the cable/MMDS and cable/SMATV cross-ownership restrictions. In particular, we seek comment on: (1) wheth-

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[51] *See, e.g., Broadcast Attribution Further Notice* at paras. 3, 43.

er the more restrictive standard serves the purposes for which it was intended; (2) whether the more restrictive standard is over- or under-inclusive; (3) whether the more restrictive attribution standard should be revised in relation to the broadcast attribution standard; (4) whether these two attribution standards should be treated as completely separate and independent formulations; and (5) whether, in view of the purposes it serves, we should require a more compelling showing b efore modifying the more restrictive standard.

15. We seek comment on whether and how any changes in our cable attribution rules should affect our various definitions of "affiliate."[52] In particular, we seek comment on whether and how those affiliation rules that are expressly based on our cable attribution rules should change if the underlying attribution rules are changed.

16. We seek comment as to the business arrangements involved in recent cable system partnerships, joint ventures, swaps, transfers, mergers and acquisitions, particularly those transactions announced or consummated in 1997 or thereafter, including those discussed in the Commission's 1997 annual report on the status of competition in the delivery of video programming.[53] Commenters should identify the entities involved in each transaction, the projected date of consummation, details of the new structure including: the percentage and nature (e.g., voting or non-voting, limited or general partnership, insulated or non-insulated, rights of conversion) of each entity's ownership interests, the number of officers, directors, and other key personnel appointed by each entity to a management committee, board or other governing body, the portion of the equity or debt financing contributed by each entity, and any authority or power held by each entity to review, veto or otherwise influence the management or operation of the cable systems, as well as the ability to purchase

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[52] *See, e.g.*, 47 C.F.R. §§ 76.924(i), 76.970(b), 76.1500(g), 76.1401(b).

[53] *Fourth Annual Report, In the Matter of Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, FCC 97-423, CS Docket No. 97-141 at ¶¶ 142-148 (rel. Jan. 13, 1998).

programming, technology, or equipment under common contract terms. We seek information, in particular, as to any business arrangements undertaken to insulate one or more parties to these transactions from control or influence over key business aspects of the cable systems at issue. We also seek comment as to the development of the Commission's cable attribution rules to avoid inconsistency with any other statutes or regulations (e.g., those of the Internal Revenue Service or the Financial Accounting Standards Board) that may influence the structuring of the business arrangements at issue.

17. With respect to each ownership or relational interest discussed herein, we seek comment on whether the specified level or degree of ownership interest in, or relationship to, an entity would be likely to impart the ability to influence or control the operations of that entity, including core areas such as budget, personnel, programming, technology, or competitive practices, such that the ownership rules should be implicated. Consistent with the purpose of Section 257 of the 1996 Act to reduce market entry barriers for small businesses,[54] we also seek comment on the impact that any changes to our cable ownership attribution or affiliation standards will have on market entry barriers for small businesses. We ask interested parties to support their comments with empirical data and economic analyses regarding levels of influence in business organizations and current market conditions.

III. CONCLUSION

18. The cable attribution rules play a crucial role in the Commission's effort to ensure a competitive, diverse, and fair video marketplace. The purpose of this review is to examine whether our current cable attribution rules are accomplishing those goals, and to determine whether fewer, additional or different restrictions are warranted.

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[54] *See* 47 U.S.C. § 257.

VII. ORDERING CLAUSES

36. Accordingly, IT IS HEREBY ORDERED that pursuant to the authority in Sections 4, 303, 612, 613, 616, 623, 628, and 653 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154, 303, 532, 533, 536, 543, 548, 572 and 573, NOTICE IS HEREBY GIVEN of proposed amendments to Part 76, in accordance with the proposals, discussions, and statement of issues in this *Notice of Proposed Rulemaking*, and that COMMENT IS SOUGHT regarding such proposals, discussion, and statement of issues.

37.IT IS FURTHER ORDERED that the Commission's Office of Public Affairs, Reference Operations Division, shall send a copy of this *Notice of Proposed Rulemaking*, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. §§ 601 *et seq.* (1981).

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Section 11(c)	)	
of the Cable Television Consumer Protection		
and Competition Act of 1992 92-264	)	MM Docket No. 92-264
	)	
Horizontal Ownership Limits	)	

MEMORANDUM OPINION AND ORDER ON RECONSIDERA TION AND FURTHER NOTICE OF PROPOSED RULEMAKING

Adopted: June 23, 1998 Released: June 26, 1998
Comment date: August 14, 1998
Reply comment date: September 3, 1998

By the Commission: Commissioner Furchtgott-Roth issuing a separate statement; Commissioner Tristani dissenting in part and issuing a separate statement.

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Appendix A: List of Commenters

I. INTRODUCTION

1. This *Second Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking* ("*Second Order on Reconsideration*" or "*Further Notice*") addresses petitions for reconsideration of the *Second Report and Order* in MM Docket No. 92-264[1] ("*Second Report and Order*") filed by the Center for Media Education/Consumer Federation of America ("CME/CFA") and Bell Atlantic Corporation ("Bell Atlantic").[2] Among other things, the *Second Report and Order*

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[1]8 FCC Rcd 8565 (1993).

[2]Petition for Reconsideration of Center for Media Education & Consumer Federation of America (filed Dec. 15, 1993); Petition of Bell Atlantic for Limited Reconsideration (filed Dec. 15, 1993).

promulgated rules pursuant to Section 613 of the Communications Act, which requires the Commission to "prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such a person, or in which such a person has an attributable interest" ("horizontal ownership rules").[3] The Commission's horizontal ownership rules established in the *Second Report and Order* provide that "no person or entity shall be permitted to reach more than 30% of all homes passed nationwide through cable systems owned by such person or entity or in which such person or entity holds an attributable interest."[4] In addition, ownership of cable systems that reach up to 35% of all homes passed nationwide is permitted "provided the additional cable systems, beyond 30% of homes passed nationwide, are minority-controlled."[5]

2. In the *Second Report and Order*,[6] the Commission voluntarily stayed the effective date of the horizontal ownership rules pending final judicial resolution of the District Court decision in *Daniels Cablevision, Inc. v. United States*,[7] which held that the underlying statute violates the First Amendment. The *Daniels* court expressly recognized that "there is substantial ground for difference of opinion" as to the constitutionality of the underlying statute, meriting an

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[3]Section 613 was adopted as Section 11(c) of Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460, 47 U.S.C. § 533(f)(1)(A).

[4]47 C.F.R. § 76.503. As specified under 47 C.F.R. § 76.503, note 1 (c), "Attributable Interest" is defined by reference to the criteria set forth in the Notes to the Commission's cable cross-ownership rules, 47 C.F.R. § 76.501.

[5]47 C.F.R. § 76.503(b). For purposes of this regulation, "minority-controlled" is defined as "more than 50% owned by one or more members of a minority group." 46 C.F.R. § 76.503, note 1(a).

[6]*Second Report and Order* at ¶ 3.

[7]*Daniels Cablevision, Inc. v. United States*, 835 F. Supp. 1, 10 (D.D.C. 1993), *aff'd in part, rev'd in part, Time Warner Entertainment Co., L.P. v. FCC*, 93 F.3d 957 (D.C. Cir. 1996).

immediate appeal of its judgment.[8] Accordingly, rather than enjoining the Commission from adopting and enforcing horizontal ownership rules, the court stayed further court proceedings, including determination and imposition of relief for the plaintiffs, pending appeal.[9] On December 15, 1993, CME/CFA moved that the Commission lift its administrative stay.[10] The following month, Time Warner challenged the stayed rules in the D.C. Circuit Court in *Time Warner Entertainment Co., L. P. v. FCC.*[11] In August 1996, the D.C. Circuit Court consolidated the *Daniels* appeal regarding the facial validity of the statute and the *Time Warner* challenge to the Commission's rules, and determined to hold court proceedings in abeyance while the Commission reconsidered the horizontal ownership rules.[12]

3. In this *Second Order on Reconsideration*, the Commission maintains the current 30% horizontal ownership limit and denies the motion to lift the voluntary stay on enforcement of that limit. We note that, while the most established programmers can obtain favorable terms from even the large cable multiple system operators ("MSOs"), the cable horizontal ownership rules remain necessary to prevent MSOs from exercising market power against new, independent, and less prominent programmers.[13] In order to facilitate monitoring of cable ownership interests, the Commission hereby lifts the voluntary stay insofar as it applies to the information reporting requirements of 47 C.F.R. § 76.503(c). Prior to acquiring attributable interests in any

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[8] *Id.* at 12.

[9] *Id.*

[10] CME/CFA Motion to Lift Stay (filed Dec. 15, 1993).

[11] *Time Warner Entertainment Co., L. P. v. FCC*, No. 94-1035 (D.C. Cir. 1994).

[12] *Time Warner Entertainment Co., L.P. v. FCC*, 93 F.3d 957, 979-80 (D.C. Cir. 1996).

[13] The consequent growth of these alternative programmers ultimately may help to check the exercise of market power by the most established programmers.

additional cable systems, a person holding an attributable interest in cable systems reaching 20% or more of homes passed nationwide will be required to notify the Commission of the incremental change the acquisition makes in terms of the 30% of homes passed standard, i.e. specifying the ownership in terms of homes passed before and after the acquisition is complete.

4. In the *Further Notice*, we seek comment on possible revisions of the horizontal ownership rules and the method by which horizontal ownership is calculated. Specifically, we ask whether changes are needed to provide a more accurate measure of horizontal concentration to reflect changes in the market as alternative MVPDs continue to grow in the future. The *Further Notice* seeks comment on two possible changes in the manner that the rules are applied: (1) whether the rules should consider the presence in the market of all MVPDs rather than cable operators alone; and (2) whether the rules should be based on actual subscribers rather than on homes passed. Specifically, comment is sought on whether the rules should provide that the number of cable subscribers an entity is authorized to reach through cable systems, when combined with the number of subscribers reached by that entity through other MVPD systems, may not exceed 30% of all MVPD subscribers nationwide.

II. BACKGROUND

5. The 1992 Cable Act and its legislative history indicate heightened Congressional concern regarding horizontal concentration among cable multiple system operators. Witnesses at the Congressional hearings, including representatives of the MSOs themselves, testified to the need for cable horizontal ownership limits to preserve competition and protect the public interest.[14] Section 613(f) of the Communications Act (Section 11(c) of the 1992 Cable Act) requires that the Commission, "[i]n order to enhance effective competition . . .

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[14]*See, e.g., Report of the Senate Committee on Commerce, Science and Transportation*, S. Rep. No. 92, 102d Cong., 1st Sess. 34 (1991) ("Senate Report") (testimony of John Malone, TCI Chairman, regarding need for cable horizontal ownership limits).

prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such a person, or in which such a person has an attributable interest."[15]

6. In adopting Section 613, Congress also recognized that multiple system ownership can benefit consumers. The House Report stated that cable industry consolidation has benefited consumers by allowing efficiencies in the administration, distribution and procurement of programming, and also noted that concentration of cable MSOs may help promote the introduction of new programming services by providing capital and a ready subscriber base for new services.[16] The House Report also observed that large cable MSOs can take competitive and programming risks that smaller operators cannot.[17] Similarly, the Senate Report acknowledged that horizontal concentration can create efficiencies from lower transaction costs in carriage negotiations between programmers and cable operators.[18]

7. Recognizing these conflicting factors, Congress directed in Section 613(f)(2) that, in addition to other public interest concerns, the Commission must consider and balance seven particular public interest objectives:

(1) to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer;

(2) to ensure that cable operators do not favor affiliated video programmers in determining carriage and do not unreasonably restrict the flow of video programming

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[15]47 U.S.C. § 533(f)(1)(A).

[16]*Report of the House Committee on Energy and Commerce*, H.R. Rep. No. 102-628, 102d Cong., 2d Sess. 43 (1992) ("House Report").

[17]*Id.*

[18]Senate Report at 33.

of affiliated video programmers to other video distributors;

(3) to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise, joint ownership of cable systems and video programmers, and the various types of non-equity controlling interests;

(4) to take into account any efficiencies and other benefits that might be gained through increased ownership or control;

(5) to make rules and regulations that reflect the dynamic nature of the communications marketplace;

(6) to impose no limitations that prevent cable operators from serving previously unserved rural areas;

(7) to impose no limitations that will impair the development of diverse and high quality programming.[19]

8. Based on an assessment of these factors, in the *Second Report and Order*, the Commission adopted a horizontal ownership

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[19]47 U.S.C. § 533(f)(2). Beginning in 1994, the Commission has issued annual reports on the status of competition in the delivery of video programming. In these annual *Competition Reports*, the Commission has noted the potential benefits as well as the potential competitive concerns of increased national horizontal concentration among cable MSOs. *See First Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 94-235, CS Docket No. 94-48, 9 FCC Rcd 7442 at ¶¶ 148-155 (1994) ("*1994 Competition Report*"); *Second Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 95-491, CS Docket No. 95-61, 11 FCC Rcd 2060 at ¶¶ 131, 146 (1995) ("*1995 Competition Report*"); *Third Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 96-496, CS Docket No. 96-133, 12 FCC Rcd 4358 at ¶¶ 138-139 (1997) ("*1996 Competition Report*"); *Fourth Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 97-423, CS Docket No. 97-141 at ¶¶ 140-14, 149 (rel. Jan. 13, 1998) ("*1997 Competition Report*").

limit prohibiting any person from having an attributable interest in cable systems that in the aggregate reach more than 30% of cable homes passed nationwide. We found that this 30% ownership limit struck the proper balance between (1) ensuring that the structure of the cable industry nationwide limited the possibility that large cable MSOs might exercise excessive market power in the purchase of video programming, and (2) ensuring that the majority of MSOs could continue to expand and benefit from the economies of scale necessary to encourage investment in new video programming services, diverse program offerings, and the deployment of advanced cable technologies.[20] In order to promote minority ownership and diversity, we also adopted the minority-control allowance, which allows an MSO to reach an additional 5% of homes passed by cable nationwide if these homes are reached by cable systems that are more than 50% owned by one or more members of a minority group.[21]

III. ISSUES ON RECONSIDERATION

A. Requests to Lower the Current 30% Ownership Limit

9. In its reconsideration petition, CME/CFA requested that the Commission lower the current limit on the number of homes passed by cable systems owned by any one entity from 30% to 10%-20%.[22] Viacom, in its comments, argued for a 15% limit.[23] The arguments raised by CME/CFA and Viacom against the Commission's 30% limit fall into five broad categories -- consideration of diversity issues; alteration of the status quo; divestiture by Tele-Communications, Inc. ("TCI"); current levels of horizontal concentration; and impact of other statutes and rules. We address the arguments for each category below.

1. Consideration of Diversity Issues

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[20] *Second Report and Order* at ¶ 25.

[21] *Id.* at ¶ 28.

[22] CME/CFA Petition at 4.

[23] Viacom Comments on CME/CFA Petition at 2.

a. Background

10. CME/CFA argued that the Commission did not give sufficient consideration to media diversity concerns in setting the 30% limit and that "[p]romoting First Amendment diversity may well require limits below that needed to address anticompetitive concerns alone."[24]

11. Opposing reconsideration of the 30% limit, TCI noted that the CME/CFA diversity argument does not even attempt to balance the pros and cons of horizontal concentration, as the Commission is required to do by Section 613. TCI noted that Congress, the Commission, the courts, and antitrust scholars and economists uniformly have recognized that horizontal ownership can enhance consumer welfare and that this enhancement must be considered in addition to diversity aims. CME/CFA's diversity argument focuses only on the potential negative consequences of horizontal concentration.[25]

b. Discussion

12. Congress specifically directed that the Commission "impose no limitations that will impair the development of diverse and high quality programming."[26] Promoting diversity of ownership has

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[24]CME/CFA Petition at 3-4.

[25]TCI Opposition to CME/CFA Petition at 2-3.

[26]47 U.S.C. § 533(f)(2)(G); *see also* House Report at 42-43 ("[D]iversity of information sources can only be assured by imposing limits on the ownership of media outlets that are substantially below those that a traditional antitrust analysis would support"); Senate Report at 32 ("[T]here are special concerns about concentration of the media in the hands of a few who may control the dissemination of information. The concern is that the media gatekeepers will (1) slant information according to their own biases, or (2) provide no outlet for unorthodox or unpopular speech because it does not sell well, or both.").

been a long-standing policy of the Commission.[27] Diversity of information sources and viewpoints can be threatened by substantial concentration among cable system operators. Moreover, as the Commission has found, entry by new MVPDs is neither cheap nor easy and cable system operators remain the dominant distributors of video programming.[28] As a result, decreases in diversity of information sources or viewpoints that accompany increased concentration among purchasers of programming may not be easily remedied.

13. Diversity is not the sole factor the Commission must consider in promulgating the cable horizontal ownership limits. As indicated above (paragraph 7), Section 613 lists seven public interest factors that the Commission must balance in making a decision.[29] Before reaching a determination that 30% was a proper limit, the Commission twice requested public comment regarding the benefits and problems of horizontal concentration among cable MSOs.[30] In addition to considering diversity aims, the Commission considered the possibility that large MSOs might have the ability to preclude the launch of new video programming services (as required by public interest factors (1) and (2) above), the benefits and efficiencies that result from horizontal concentration (as required by public interest

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[27]For a broad assessment of the Commission's diversity analysis in the mass media context, *see Further Notice of Proposed Rule Making, Review of the Commission's Regulations Governing Television Broadcasting*, MM Docket No. 91-221, 10 FCC Rcd 3524 at ¶¶ 54-80 (1994).

[28]*1997 Competition Report* ¶¶ 126, 128, 150.

[29]*See* 47 U.S.C. § 533(f)(2).

[30]*See Notice of Proposed Rule Making and Notice of Inquiry, Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd 210 at ¶ 37 (1992) ("*First Notice and NOI*"); *Report and Order and Further Notice of Proposed Rule Making, Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd 6928 at ¶¶ 139-52 (1993) ("*First Report and Further Notice*").

factor (4)), and the relative impact of other statutes and rules in addressing competitive concerns regarding large MSOs.[31] In the *Second Report and Order*, the Commission specifically noted that Section 19 of the 1992 Cable Act (the program access requirements), Sections 4 and 5 of the 1992 Cable Act (the must-carry requirements), and Section 612 of the Communications Act (the leased access requirements), combined with the 30% ownership limit, "will be appropriate to address the diversity aims which underlie the statutory horizontal ownership provisions."[32] The Commission also considered diversity in allowing ownership of additional cable systems up to 35% of cable homes passed, provided the additional cable systems are minority-controlled.[33]

14. We believe the 30% horizontal ownership limit adopted by the Commission provides considerable protection for diversity concerns. The record in this docket clearly demonstrates that the Commission took into consideration diversity concerns in adopting the 30% cable horizontal ownership limits. The Commission balanced those considerations, as required by Section 613, with many other factors, some of which support the growth of cable MSOs. In fact, the Commission's consideration of diversity concerns is reflected by the fact that we adopted a horizontal ownership limit lower than one that might have been indicated by a traditional antitrust analysis alone.[34] The Commission was concerned that a lower horizontal ownership limit could "impair the development of diverse and high quality

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[31] *Second Report and Order* at ¶¶ 25-26.

[32] *Id.* at ¶ 26.

[33] *Id.* at ¶ 28.

[34] House Report at 42-43. In monopolization cases, the burden is on the plaintiff to prove that the defendant has monopoly power and this "virtually never" occurs when a defendant has a market share less than 50%. ABA Section of Antitrust Law, *Antitrust Law Developments (Fourth)* 236 (1997).

programming."[35] The Commission properly concluded that a 30% limit is generally appropriate to prevent the largest MSOs from gaining excessive leverage, and also ensures that the majority of MSOs continue to expand and obtain the economies of scale necessary to encourage investment in new video programming services and the deployment of advanced cable technologies.[36]

2. Alteration of the Status Quo

a. Background

15. CME/CFA asserted that the 30% horizontal ownership limit is too high because it does not alter the status quo. CME/CFA contended that the Commission "failed to acknowledge that existing levels of horizontal concentration are too high," citing a passage from the Senate Report stating that large MSOs have market power vis-a-vis programmers.[37] Arguing that Congress had made a specific finding that MSOs have the power to exact equity from programmers in exchange for carriage, CME/CFA asserted that Congress sought to change the status quo in the 1992 Cable Act.[38] In their reply comments, CME/CFA argued, without citing any specific legislative history, that the 1992 Cable Act was intended to reverse the Commission's decision in the *1990 Cable Report* not to adopt ownership limits.[39] CME/CFA stated that the 30% limit in the *Second Report and Order* resembles the balance struck by the Commission in its *1990 Cable Report* more than those envisioned in the 1992 Act, and that the *Second Report and Order* substituted the *1990 Cable Report* judgment for the requirements of the

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[35]47 U.S.C. § 533(f)(2)(G).

[36]*Second Report and Order* at ¶ 25.

[37]CME/CFA Petition at 4 (citing Senate Report at 24, 33).

[38]*Id.* at 4-11.

[39]CME/CFA Reply to Oppositions at 2-4 (citing *Rate Deregulation & the Commission's Policies Relating to the Provision of Cable Television Serv., Report on Competition*, 5 FCC Rcd 4962 (1990) ("*1990 Cable Report*")).

1992 Cable Act.[40]

16. Time Warner Entertainment Co., L.P. ("Time Warner") and the National Cable Television Association ("NCTA") argued the Commission was given the discretion to balance competing concerns by Congress and disagreed that the 1992 Cable Act requires the Commission to alter the status quo.[41]

b. Discussion

17. The issue here is one of statutory interpretation -- whether Congress, in enacting Section 613, made a final determination that then current levels of horizontal concentration were too high, requiring the Commission to adopt rules to force divestiture and to reduce horizontal concentration. We believe that the text of Section 613 is clear that the Commission was given the discretion to adopt limits that may or may not require divestiture.

18. Section 613 gives the Commission the discretion "to prescribe rules and regulations establishing *reasonable limits* on the number of cable subscribers a person is authorized to reach ...."[42] CME/CFA's argument ignores that the statute does not direct the Commission to alter the status quo by ordering divestiture by any cable MSO. Instead, Congress required that the Commission set "reasonable limits" and left the parameters of what "reasonable limits" would be to Commission discretion.

19. Further, we note that this construction of the statute is supported by the legislative history. The Senate Report explicitly states that "[t]he legislation does not imply that any existing company must be divested and gives the FCC flexibility to determine what limits are

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[40]*Id.* at 2-4.

[41]Time Warner Opposition to CME/CFA Petition at 7-8; NCTA Opposition to CME/CFA Petition at 7-8.

[42]47 U.S.C. § 533(f)(1)(A) (emphasis added).

reasonable."[43] The House Report states that: "Currently, the largest MSO controls access to almost 25 percent of all US cable subscribers. Although this percentage may appear low relative to other industries, the Committee believes that it may be quite significant depending on the subscriber level needed to launch and sustain a cable programming service."[44] The language of the House Report is significant on this point. While it demonstrates Congress' concern about current levels of horizontal concentration, it expressly does not make a final conclusion, but simply states that current levels "may be quite significant depending on" the number of subscribers needed to launch and sustain a programming service.[45]

20. The statute and the legislative history make clear that the Commission was not required to alter current industry structure, but to consider the potential public interest concerns associated with the industry structure. The Commission fully considered such interests.

3. Divestiture by TCI

a. Background

21. CME/CFA asserted that the *Second Report and Order* was too concerned about avoiding divestiture by TCI and was not focused on consumer welfare.[46] Arguing that the legislative history of Section 613 indicates that divestiture might be warranted, CME/CFA contended that a passage in the Senate Report stating that the legislation "does not imply that any existing company must be divested" expressly left open the possibility of divestiture.[47] CME/CFA urged that the Commission not be deterred from imposing horizontal limits which

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[43]Senate Report at 34.

[44]House Report at 42.

[45]*Id.*

[46]CME/CFA Petition at 4-11.

[47]*Id.* (quoting Senate Report at 34).

would require TCI to divest, as Congress required the Commission to weigh seven public interest considerations, none of which was to ensure that MSOs could continue to expand.[48]

22. Viacom agreed with CME/CFA that the *Second Report and Order* placed too much reliance on language in the Senate Report which states that the limit "does not imply that any existing company must be divested." Viacom argued that the legislative history does not prohibit the Commission from adopting a limit that would require divestiture, but, at most, only indicates that the Commission should not promulgate rules which would impose divestiture if the divestiture were not in the public interest. Viacom stated that divestiture is relevant and should be considered by the Commission in adopting horizontal ownership rules, but that avoiding divestiture should not override the public interest concern regarding excess MSO market power against unaffiliated programmers.[49]

23. Time Warner, TCI, Liberty Media Corporation ("Liberty Media"), and NCTA responded that the Commission's decision not to order divestiture by TCI was based upon the finding that there was an "absence of definitive evidence that existing levels of ownership are sufficient to impede the entry of new video programmers or have an adverse effect on diversity."[50] Liberty Media argued that, since no programmer claimed in the original proceeding that any cable operator had exercised horizontal market power and no commenter introduced empirical evidence of such power, it was proper for the Commission to make this finding.[51] NCTA argued that avoiding divestiture was not the driving factor in the Commission's decision, as the Commission

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[48]CME/CFA Reply at 2-4.

[49]Viacom Comments at 7-8.

[50]Time Warner Opposition at 7-8; NCTA Opposition at 7-8; Liberty Media Reply at 9-11 (quoting *Second Report and Order* at ¶ 27).

[51]Liberty Media Reply at 9-11.

considered a number of factors in proposing and adopting the limits, including avoiding potential disruption in existing ownership and the absence of definitive evidence that existing levels of ownership are harmful.[52]

b. Discussion

24. We agree with Viacom and CME/CFA that the Commission has the authority under Section 613 to order divestiture. We disagree with CME/CFA to the extent they argue that the Commission should not consider the full impact divestiture would entail before promulgating such rules. Inquiry into the impact divestiture would have upon subscribers, programmers and industry investment are legitimate public interest objectives that the Commission is entitled to consider. A rule requiring divestiture must be based on consideration of all relevant factors.[53] We believe that the *Second Report and Order* properly considered whether the substantial structural change that divestiture would entail was warranted.

25. We reject CME/CFA's argument that the impact of ordering divestiture should not have entered into the Commission's decision-making because it is not one of the seven specifically-enumerated public interest factors of Section 613. The statute explicitly contemplates that the factors enumerated are "among other public interest objectives" that the Commission is to consider.[54] Assessing the impact

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[52]NCTA Opposition at 7-8 (quoting *Second Report and Order* at ¶ 27); NCTA Reply Comments at 3-4.

[53]In *Citizens to Preserve Overton Park, Inc. v. Volpe*, 401 U.S. 402 (1971), the Supreme Court held that courts reviewing agency action under the arbitrary and capricious standard must make a "searching and careful" examination of "whether the decision was based on a consideration of the relevant factors. . . ." *See also Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 850-53 (D.C. Cir. 1970), *cert. denied*, 403 U.S. 923 (1971) (the function of a reviewing court "is to assure that the agency has given reasoned consideration to all the material facts and issues").

[54]47 U.S.C. § 533(f)(2); *see Greater Boston Television*, 444 F.2d at 850-53 ("Assuming consistency with law and the legislative mandate, the agency has latitude not merely

of divestiture is consistent with Section 613's directive that the Commission "take particular account of the market structure" and "not impose limitations which would impair the development of diverse and high quality video programming."[55]

26. In both the *First Report and Further Notice* and the *Second Report and Order*, the Commission considered arguments for low limits that would require divestiture. The Commission based its final decision not solely on a determination to avoid divestiture, as CME/CFA suggested, but, more importantly, upon the public interest requirements of Section 613. In its initial comments, the Association of Independent Television Stations, Inc. argued for a 10% subscriber cap.[56] In the *First Report and Further Notice*, the Commission stated that this proposal not only would require divestiture but "would sacrifice the efficiencies achieved by horizontal concentration."[57] The Commission determined that the proposal would "be contrary to the legislative history" of Section 613.[58] The Commission asked in the *First Report and Further Notice* that parties "favoring limits below 25%" that would require divestiture "discuss the effect that such divestiture would have on service to subscribers, programming carriage agreements, and on future MSO investment in new programming and technology."[59] The Commission emphasized the over-arching importance of striking "the proper balance among the competing public interest objectives Congress directed us to consider" in setting the horizontal ownership limit,

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to find facts and make judgments, but also to select the policies deemed in the public interest.").

[55]47 U.S.C. §§ 533(f)(2)(C), (E), (G).

[56]*See* Association of Independent Television Stations, Inc. Initial [Feb. 1993] Comments at 7; *First Report and Further Notice* at ¶ 146.

[57]*First Report and Further Notice* at ¶ 148.

[58]*Id.*

[59]*Id.* at ¶ 149.

without excluding the possibility of divestiture.[60]

27. In the *Second Report and Order*, the Commission again considered proposals that would have required divestiture by the largest MSO, TCI, and also discussed the other effects divestiture would create. The Commission, after considering the "statutory factors and . . . the preponderance of the data provided in the record," concluded that a 30% limit was appropriate because it would "prevent the nation's largest MSOs from gaining enhanced leverage from increased horizontal concentration" while "ensur[ing] that the majority of MSOs continue to expand and benefit" from the positive aspects of increased concentration.[61] The Commission expressly confronted the divestiture issue and explicitly determined that "in the absence of definitive evidence that existing levels of ownership are sufficient to impede the entry of new video programmers or have an adverse effect on diversity, existing arrangements should not be disrupted."[62]

4. Current Levels of Horizontal Concentration

a. Background

28. CME/CFA asserted that the *Second Report and Order* did not sufficiently address the evidence that the largest MSO, TCI, already has market power and uses its market power to disadvantage competing program services.[63] CME/CFA argued that, from a competitive standpoint, the Commission "fail[ed] to acknowledge that existing levels of horizontal concentration are too high."[64]

29. Viacom argued that a lower limit is needed because, based upon its own experience, 40 million subscribers are necessary for an advertising-supported, basic cable programming network to be

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[60] *Id.* at ¶ 134.

[61] *Second Report and Order* at ¶ 25.

[62] *Id.* at ¶ 27.

[63] CME/CFA Petition at 4-11.

[64] *Id.* at 2-4.

successful.[65] Viacom extrapolated from this figure its argument that no MSO should be allowed to come close to controlling access to enough subscribers that would prevent a programmer from reaching 40 million homes -- i.e., based on 1993 cable subscribership figures, no MSO should be allowed to come close to controlling access to 30.9% of cable subscribers. Viacom also asserted that the then current levels of market concentration allowed large MSOs to drive down the license fees they pay to programmers. This, Viacom argued, affects the entire market for license fees and drives them down across the board. The result is that programmers cannot spend as much on development, thus potentially reducing the diversity and quality of programming available to subscribers.[66]

30. Both CME/CFA and Viacom provided anecdotal evidence to support their belief that TCI, the nation's largest MSO, is too large. CME/CFA cited the Federal Trade Commission's ("FTC") agreement with TCI and Liberty Media forcing divestiture of QVC, Inc. ("QVC") as evidence that TCI possesses currently anticompetitive influence resulting from its large horizontal size.[67] In addition, CME/CFA cited Viacom's antitrust complaint against TCI and claimed that, according to the Viacom complaint, TCI had dropped Viacom's The Movie Channel in favor of TCI affiliate Encore Media, and had withheld affiliation with Viacom's Showtime to force Showtime either to merge with Encore Media or be destroyed.[68] CME/CFA asserted

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[65]Viacom Comments at 9. Viacom estimated that 40 million subscribers equaled approximately 69.1% of cable subscribers nationwide at the time of Viacom's filing. *Id.*

[66]*Id.*

[67]CME/CFA Petition at 7-8 (citing *TeleCommunications, Inc., et al.; Proposed Consent Agreement with Analysis to Aid Public Comment*, 58 Fed. Reg. 63167 (Nov. 30, 1993)).

[68]*Id.* at 8-9 (citing *Viacom International, Inc. v. Telecommunications, Inc., Liberty Media, et. al*, Civ. No. 93-CIV6658(KC) (filed S.D.N.Y. Sept. 23, 1993));

that, if TCI can wield power over Viacom and its popular networks, it certainly has power to preclude the launching of new programming from smaller programmers.[69] CME/CFA also cited a passage in the Senate Report stating that "[w]itnesses at the hearings testified that. . . [MSOs have the power] to determine what programming services can 'make it' on cable."[70] CME/CFA argued that independent programmers' failure to argue for lower levels of concentration previously in this docket indicates "their reasonable fear of offending the MSOs who, after all, have it in their power to put them out of business."[71]

31. Viacom stated that TCI's anticompetitive conduct led Viacom, after the initial comment periods in this proceeding closed, to file its antitrust complaint against TCI, Liberty Media and others and also convinced Viacom that stricter horizontal rules are necessary to prevent anticompetitive conduct in the market for programming services.[72]

32. All other cable operators filing comments strenuously opposed the argument that current levels of horizontal concentration are "too high." TCI stated that the arguments of CME/CFA and Viacom fail to recognize the current benefits of horizontal concentration, which the Commission is required to consider under its statutory mandate.[73] TCI also asserted that horizontal concentration allows

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CME/CFA Reply at 3.

[69]CME/CFA Petition at 7-11; CME/CFA Reply at 3.

[70]*Id.* (quoting Senate Report at 33).

[71]CME/CFA Petition at 3, 7-11.

[72]Viacom Motion for Leave to File Response and Response at 2-3. Pursuant to Section 1.415(d) of the Commission's rules, we deny Viacom's motion to submit its late-filed response. However, we will consider Viacom's response as informal comments under Section 1.419(b).

[73]TCI Opposition at 2-3.

MSOs to achieve economies of scale in research and development of transmission and distribution technology and achieve considerable savings in administrative costs such as billing operations, advertising, marketing, and management. In addition, Time Warner stated that the costs of negotiating with programmers are reduced on both sides of the table.[74]

33. TCI argued that under traditional antitrust analysis, the then current ownership level of MSOs did not equate to high concentration, citing legislative history which reported that the Herfindahl-Hirshman Index ("HHI") of the top 20 MSOs was 491 and the Four-Firm Ratio was 36%, well below the Department of Justice thresholds of 1,000 and 50%. TCI stated that these levels did not indicate that MSOs are able to extract unreasonable concessions from their suppliers.[75] Time Warner pointed out that an MSO's incentive to undertake a foreclosure strategy is counterbalanced by desires to increase subscribership and decrease churning of programming.[76] TCI also submitted a report from a group of economists that recommended against setting low ownership limits because, due to MSOs' recognition that their own success depends on the availability of a high quantity and quality of programming, increased concentration "will not affect the array of programming selected and distributed by the cable operator and therefore will not distort the allocation of resources in the production of program services."[77]

34. Cable MSOs and programmers also strongly disputed Viacom's suggestion that 40 million subscribers are required for suc-

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[74]Time Warner Opposition at 3-5; *see also* House Report at 43.

[75]*See* TCI Opposition at 4-5.

[76]Time Warner Opposition at 8-9; *see also* Senate Report at 24.

[77]Stanley M. Besen, Steven R. Brenner and John R. Woodbury, *An Economic Analysis of the FCC's Proposed Cable Ownership Restrictions* at 19-22 (attached to TCI Opposition).

cess. Several pointed out that a number of successful cable networks had never achieved penetration levels above 60% to 70%.[78] Time Warner argued that there is no "magic" level of penetration that necessarily assures, or prevents, a programming service's commercial success.[79] Turner Broadcasting System, Inc. ("TBS") pointed out in its opposition that ESPN2, an unaffiliated programmer, already had over 10 million subscribers, one million more than the vertically affiliated Cartoon Network, and the then-unaffiliated Sci-Fi Channel was regarded as successful with 15 million subscribers.[80] Liberty Media stated that 46 of the 68 listed national basic cable networks then had fewer than 40 million subscribers.[81]

35. TCI and Liberty Media responded to CME/CFA and Viacom's specific charges of anticompetitive conduct by arguing that the charges were unsupported. TCI argued that the consent decree cannot be used as evidence against TCI. TCI also stated that no competitive problems were ever proved in the QVC matter and that TCI divested its interest solely because it did not want to interfere with QVC's tender offer for Paramount.[82] Liberty Media argued that the agreement with the FTC was intended to address vertical concerns and

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[78]*See* Time Warner Opposition at 6-7 (BET and Country Music Television in operation for years with levels below 60-70%).

[79]Time Warner Reply to Viacom Comments at 6; Time Warner Opposition at 6-7.

[80]TBS Opposition to CME/CFA Petition at 2.

[81]Liberty Media Opposition at 10-11.

[82]*See* Testimony of John C. Malone (TCI Chairman and CEO) before the Senate Subcommittee on Antitrust, Monopolies and Business Rights (Dec. 16, 1993) (attached to TCI Opposition).

not horizontal size.[83] TCI and Liberty Media stated that Viacom's antitrust suit was filed in the context of its attempt to prevent QVC from acquiring Paramount. Given this history, TCI and Liberty Media argued that it would be improper for the Commission to decide its cable horizontal ownership limits based upon unproven allegations made by a competitor with the desire to enhance Viacom's efforts to increase its own ownership concentration in several markets.[84] TBS discounted Viacom's allegations against TCI as "an extension of its current jihad with TCI."[85] Time Warner stated that Viacom's argument consists of unproven allegations.[86]

36. Time Warner also pointed out that during the prior comment period, no programmer, either failed or successful, proposed or well-established, claimed that any cable operator exercised horizontal market power, and no commenter introduced any empirical evidence of the exercise of such market power.[87] Liberty Media argued that without this evidence, the Commission appropriately determined that cable horizontal ownership limits that freeze or reduce existing ownership levels were unjustified.[88]

b. Discussion

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[83] *See* Liberty Media Opposition at 9, quoting Statement of Mary Lou Steptoe before the Senate Subcommittee on Antitrust, Monopolies and Business Rights, Committee on the Judiciary 5-6 (Nov. 18, 1993) ("Since the alleged competitive problems stem from the vertical link between TCI/LMC and QVC, the FTC's consent order addresses them by severing that link.").

[84] TCI Opposition at 6-7; Liberty Media Opposition at 8-12; Liberty Media Reply at 12-15.

[85] TBS Response to Viacom's Comments at 1.

[86] Time Warner Reply at 3-5.

[87] *Id.* at 3-5.

[88] Liberty Media Opposition at 6.

37. As stated above, the Commission found in the *Second Report and Order* that 30% was an appropriate limit "in the absence of definitive evidence that existing levels of ownership are sufficient to impede the entry of new video programmers or have an adverse affect on diversity ..."[89] The legislative history of Section 613 indicates Congress' concern that excessive horizontal concentration had the potential to facilitate the anticompetitive exercise of monopsony power and adversely impact the diversity of programming.[90] Because cable MSOs generally purchase cable programming on a national level and at the same time distribute that programming to consumers on a local level through the locally franchised cable system, assessing the impact of cable concentration by examining both the national programming market and the local distribution market is appropriate. In the *Second Report and Order*, the Commission found that a 30% limit was "appropriate to prevent the nation's largest MSOs from gaining enhanced leverage from increased horizontal concentration."[91] The Commission then concluded that the 30% limit is "reasonable to prevent the types of anti-competitive conduct which concerned Congress, particularly when coupled with the behavioral restrictions contained in [the program access and program carriage provisions] .... "[92] In this reconsideration proceeding, no one has proffered any new evidence that requires the Commission to alter this finding. Moreover, we believe the 30% limit complies with the intent of Congress and satisfies the criteria specified in Section 613.

38. In enacting Section 613, Congress expressed concern about concentration of the media in the hands of a few "media gate-

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[89] *Second Report and Order* at ¶ 27.

[90] Senate Report at 32-33.

[91] *Second Report and Order* at ¶ 25.

[92] *Id.* at ¶ 26.

keepers" who could control dissemination of information.[93] The accumulation of market share on a national level by a single or small number of large cable MSOs could diminish the diversity of programming available to most households in the United States. As of June 1997, there were more than 64 million cable subscribers representing more than 66% of all television households in the United States.[94] As such, cable television remains a primary source of information and programming for many households in the United States. The 30% rule limits the extent to which one or a few large cable MSOs could reduce the diversity of programming in the United States.

39. The 30% limit diminishes the likelihood that either a large cable MSO acting unilaterally or a group of cable MSOs acting in concert could exercise market power in the purchase of programming.[95] While the exercise of market power could result in lower negotiated programming costs for these MSOs in the short run, it could also adversely affect the development of diverse and innovative programming in the long run. In addition to preserving the development of programming, the 30% limit decreases the likelihood that a large cable MSO acting unilaterally could coerce nonaffiliated programmers into denying programming to alternative MVPDs, such as a DBS provider.[96]

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[93]Senate Report at 32, 33.

[94]*1997 Competition Report* at ¶¶ 14 and 15.

[95]*See generally,* David Waterman and Andrew Weiss, VERTICAL INTEGRATION IN CABLE TELEVISION (1997) at 55-86 and 128-141.

[96]*See also* 47 U.S.C. § 548(b), which makes it "unlawful for a cable operator . . . to engage in unfair methods of competition or unfair or deceptive acts or practices, the purpose or effect of which is to hinder significantly or to prevent any multichannel video programming distributor from providing satellite cable programming or satellite broadcast programming to subscribers or consumers."

40. The 30% limit may serve to facilitate the development of competition in those markets where cable MSO market power already exists. The rule limits the extent to which large cable MSOs can merge and result in one or two MSO's controlling local cable markets nationwide. Limiting this merger potential may preserve opportunities for entry by overbuilders or other MVPD providers and reduce the likelihood that large MSOs can coordinate their behavior by mutually forbearing from overbuilding each other's service territories. Coordinated activity between cable MSOs, whether tacit or overt, is more likely with few firms than many (due to greater ease in reaching a consensus, monitoring compliance, and punishing cheaters), and such behavior will have a greater impact the larger combined share of the market these collusive firms control. The 30% limit also reduces the likelihood of coordinated activity between large cable MSOs in areas such as program purchasing and equipment purchasing (e.g., set top boxes and converters).[97]

41. The 30% limit permits cable MSOs to cluster systems in order to gain efficiencies related to economies of scale and scope in administration, deployment of new technologies and services, extension into previously unserved territories, etc..[98] Accordingly, the 30% limit simultaneously guards against the potential anticompetitive effects of horizontal concentration and allows cable MSOs to realize the benefits of clustering.

42. The 30% limit is a structural complement to the program

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[97] *See generally,* James L. Langenfeld and Louis Silvia, *Federal Trade Commission Horizontal Restraint Cases: An Economic Perspective,* ANTITRUST LAW JOURNAL (1993); Alexis Jacquemin and Margaret E. Slade, *Cartels, Collusion, and Horizontal Merger,* HANDBOOK OF INDUSTRIAL ORGANIZATION, Richard Schmalensee and Robert Willig, ed., (1990); *see also, NCAA v. University of Oklahoma,* 468 U.S. 85 (1984); *Northwest Wholesale Stationers, Inc. v. Pacific Stationary and Printing Co.,* 105 S.Ct. 2613 (1985).

[98] *E.g., Second Report and Order* at ¶¶ 25-26; *1997 Competition Report* at ¶¶ 140-148.

access provisions.[99] The horizontal ownership rules limit the potential for anticompetitive abuses of purchasing power in areas outside of the core areas covered by the program access rules, such as programming contracts between cable operators and non-vertically integrated programmers or contracts involving programming that is not delivered to cable operators via satellites. In addition, structural regulation generally is more easily enforced and detected than conduct regulation. We recognize that a large market share does not in and of itself indicate that a firm or a collection of firms has the ability to exercise market power or engage in anticompetitive behavior.[100] Nevertheless, structural regulation imposes far fewer economic costs on the market than regulatory models that use primarily price or case-specific conduct regulation as a way to mitigate strategic, anticompetitive behavior.[101]

43. It appears that the current level of concentration among cable MSOs has not prevented an expansion in programming sources and networks. The nation's largest cable MSO reached 24% of homes passed by cable in 1990;[102] grew to 27% by 1993;[103] and reached 29.32%

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[99]47 U.S.C. § 628; 47 C.F.R. § 76.1000 et seq.

[100]*See, e.g., In re Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, 11 FCC Rcd 3271 (1995). We also recognize that the courts have generally found that a firm can not successfully obtain a monopoly with less than a 30% market share. *Antitrust Law Developments (Fourth)* 298-99 and cases cited therein.

[101]*Cf., Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, *reh'g denied*, 509 U.S. 940 (1993).

[102]Senate Report at 32.

[103]*Second Report and Order* at n. 40.

at the time of the *1997 Competition Report*.[104] At the same time, our annual competition reports indicate a gradual but continuous growth and expansion in both cable-affiliated and independent programming sources and programming networks.[105] This evidence tends to suggest that the Commission properly struck a reasonable balance between concentration and diversity concerns. Thus, contrary to CFA's allegations, the actual evidence to date suggests that allowing a cable MSO to own systems reaching 30% of homes passed has not significantly hampered new video programmers' entry in the programming market.

44. Viacom's argument that 40 million subscribers are needed for a national cable programming network to be successful is not supported by the record. Other parties in the proceeding have presented evidence disputing Viacom's 40 million figure, including several examples of cable programming services (such as BET, Nickelodeon, ESPN2) that were successful before reaching 40 million subscribers. Prior comments in this docket also provide data that 40 million subscribers are not necessary for a national, basic cable programming network to be successful.[106] Commenters, including new networks, in other proceedings before the Commission likewise have

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[104] *1997 Competition Report* at Appendix E, Table E-3. Because the Commission's reporting requirements have been stayed along with the horizontal ownership limit, we currently do not have sufficient information regarding the many joint ventures and other transactions, recently announced by cable MSOs such as TCI, Cablevision, Adelphia, Falcon, Time-Warner, etc., to determine conclusively whether these transactions will result in attributable ownership interests that would place some MSOs above the 30% threshold.

[105] *Id.* at ¶ 158.

[106] *See* Time Warner Initial [Feb. 1993] Comments at 27-29 and TCI Initial [Feb. 1993] Comments at 24-25 (both listing several apparently successful national basic cable programming networks with below 40 million subscriber penetration).

stated that a new national, advertiser-supported network requires a threshold subscriber base of ten to twenty million subscribers.[107]

45. The *1997 Competition Report* estimates the total number of MVPD subscribers nationwide to be 73,646,970.[108] Consequently, a programmer that fails to sell its product to an MSO having 30% of cable homes passed nationwide still would have the opportunity to reach (through the remaining MVPDs) over 50 million subscribers, well over the threshold for national success. Many among the top 50 programmers nationwide, including MSNBC, the Disney Channel, and Turner Classic Movies, reach substantially less than 40 million subscribers.[109] Neither Viacom nor CME/CFA has provided sufficient grounds to warrant a lowering of the 30% horizontal ownership limit and freezing or reducing existing levels of cable ownership.

5. Impact of Other Statutory Provisions and Rules

a. Background

46. CME/CFA argued that the Commission's reliance in the *Second Report and Order* upon existing statutes and regulations, such as the program access and carriage rules, as a justification for higher ownership limits was improper because structural regulations provide

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[107] *See* Outdoor Life Network, Speedvision Network, The Golf Channel, BET on Jazz, and America's Health Network Comments at 11-13, 34, 36 in *Closed Captioning and Video Description of Video Programming, Implementation of Section 305 of the Telecommunications Act of 1996, Video Programming Accessibility*, MM Docket No. 95-176; Affidavit of Christopher H. Murvin at 8, Affidavit of Jefferi K. Lee at 6, and Affidavit of Roger Williams at 8 in *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation (Leased Access)*, MM Docket No. 92-266 & CS Docket No. 96-60; Program Providers Comments at 12 in *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation (Going Forward)*, MM Dockets Nos. 92-266 & 96-215.

[108] *1997 Competition Report* at Appendix E, Table E-1.

[109] *Id.* at Appendix F, Table F-6.

"a superior means of promoting diversity compared to behavioral regulations."[110]

47. Viacom also asserted that the Commission should not have relied on other sections of the 1992 Cable Act, such as program carriage and access provisions,[111] must-carry requirements,[112] channel occupancy limits,[113] and leased access requirements.[114] Viacom argued that Congress did not indicate that the Commission should calibrate the cable horizontal ownership rules to take these provisions into account, as these provisions were enacted with purposes separate from the cable horizontal ownership provision. Viacom stated that these other provisions probably will not have any practical impact on restraining anticompetitive conduct of cable operators: leased access is probably not a viable option for programmers, must-carry provisions are for television broadcasters (not unaffiliated programmers like Viacom), and the program access provisions only require MSOs to offer their own programming to other distributors. Viacom also argued that although the program carriage provisions prohibit cable operators from extracting a financial interest or exclusivity rights in exchange for programming carriage, the statute does not address the issue arising when an MSO "solely by virtue of the size of its subscriber base" has market power to determine whether a programming service can reach

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[110]CME/CFA Petition at 3. The Commission notes that in its original comments in this proceeding, CFA argued that the Commission should "proceed with great caution and consider the effect of implementation of the rate regulation and program access provisions of the 1992 Cable Act when creating rules with respect to cable ownership limits and concentration." CFA Initial [Feb. 1993] Comments at 3.

[111]47 U.S.C. §§ 536, 548.

[112]47 U.S.C. §§ 534, 535.

[113]47 U.S.C. § 533(f)(1)(B).

[114]47 U.S.C. § 532.

the critical mass of subscribers needed to succeed. Viacom also stated that programmers are not likely to bring program carriage complaints against the largest MSOs, who are their biggest customers and therefore essential to success.[115]

48. Liberty Media and Time Warner responded by arguing that the existing restrictions in the 1992 Cable Act support maintaining the 30% ownership limit. Liberty Media argued that the Commission properly considered the cumulative effect of these regulations to protect against the exertion of undue power over the success of new video services.[116] Time Warner agreed, stating that the cable horizontal ownership limits should not be viewed as an isolated measure and that the cumulative effect of all provisions and rules should be taken into account.[117] Liberty Media also pointed out that Viacom had taken completely the opposite position on this point in the initial comment round in this docket.[118] NCTA stated that Congress directed the Commission to take into account the market structure, ownership patterns and other relationships in the industry in establishing these limits, and that the Commission found that the cumulative effect of all these rules should protect against any one cable operator's exertion of excessive market power.[119]

b. Discussion

49. We believe that the *Second Report and Order* properly considered the impact of other rules and statutes since the public interest requirements of Section 613 require the Commission to examine the marketplace as it currently operates, which includes the effects

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[115]Viacom Comments at 4-5.

[116]Liberty Media Opposition to CME/CFA Petition at 6-7.

[117]Time Warner Opposition at 5.

[118]Liberty Media Reply at 5-9.

[119]NCTA Opposition at 7-8; NCTA Reply at 3-5.

of current Commission rules and statutes. Specifically, the public interest factors of Section 613 state that the Commission is to "take particular account of the market structure, ownership patterns, and other relationships of the cable television industry," "account for any efficiencies and other benefits that might be gained through increased ownership or control," "make such rules and regulations reflect the dynamic nature of the communications marketplace," and "not impose limitations which would impair the development of diverse and high quality video programming."[120]

50. Statutes and rules such as the program access, program carriage, channel occupancy limits, and must-carry requirements all affect the way the cable television industry currently operates and have a profound effect on current industry structure and performance. For example, in the *1994 Competition Report*, the Commission stated that, "[t]o the extent that large MSOs used their power over vertically-integrated programmers to obtain exclusive distribution rights to satellite-delivered programming, and those exclusive rights disadvantaged competitors of those large MSOs, the 1992 Cable Act's program access provisions and the Commission's program access rules appear to have largely addressed the problem."[121] In the *1997 Competition Report*, the Commission noted that "the program access rules have been credited as having been a necessary factor in the development of both the DBS [direct broadcast satellite] and MMDS [multichannel multipoint distribution service] industries."[122] Because these provisions have real and substantive impact upon the market, the Commission, in

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[120] 47 U.S.C. § 533(f)(2)(C), (D), (E), (G).

[121] *1994 Competition Report* at ¶ 149.

[122] *1997 Competition Report* at ¶ 230. *See also Second Report and Order* at ¶ 54 ("carriage of broadcast, PEG [public, educational, and governmental] and leased access channels promote diversity and provides alternative sources of unaffiliated programming to cable subscribers in furtherance of the statutory objectives"); *First Order on Reconsideration* at ¶ 27 (reaffirming same).

setting the horizontal ownership limit, may properly consider the impact of these provisions in alleviating some of the public interest and anticompetitive concerns about horizontal concentration.[123]

51. In addition to CME/CFA's argument that the Commission should not have placed any reliance on the impact of these other statutes and rules, both CME/CFA and Viacom argued that the Commission placed too much weight on the impact of these other statutes and rules on alleviating competitive concerns. In the *Second Report and Order*, the Commission recognized that anticompetitive concerns might indeed be present under the current market structure. The Commission did not conclude that statutory provisions and rules such as the program carriage and access provisions, the must-carry requirements, and the channel occupancy limits were sufficient by themselves to address anticompetitive concerns about horizontal concentration. The Commission did find that, when combined with these other statutory provisions and rules addressing similar concerns, the 30% horizontal ownership limit was "reasonable" and stated that: "The cumulative effect of these regulations coupled with a horizontal ownership limit of 30% should protect against any one cable system exerting undue power that could prevent the success of new video programming services or `unfairly impede the flow of video programming to the consumer.'"[124] The Commission's weighing of these other statutory provisions and rules in crafting the rules adopted in the *Second Report and Order* was appropriate.

B. Requests to Revise the Calculation Factors

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[123]To insure that our other rules have their continued efficacy, we have explored, where necessary, suitable adjustments to these rules. *See, e.g., Memorandum Opinion and Order and Notice of Proposed Rulemaking, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Petition for Rulemaking of Ameritech New Media, Inc. Regarding Development of Competition and Diversity in Video Programming Distribution and Carriage*, FCC 97-415, CS Docket no. 97-248, RM No. 9097 (rel. Dec. 18, 1997).

[124]*Second Report and Order* at ¶ 26 (quoting 47 U.S.C. § 533(f)(2)(A)).

1. Inclusion of Affiliated Telephone Companies

a. Background

52. CME/CFA requested that the Commission take into account in the calculation of "homes passed" the number of telephone households of a telephone company affiliated with an MSO. CME/CFA argued that the current regulations do not take into account proposed mergers and joint ventures between telephone companies and cable companies -- e.g., the (then) proposed merger of Bell Atlantic and TCI that would have resulted in access to 40% of all U.S. households, either through Bell Atlantic telephone lines or TCI's cable systems. CME/CFA argued that just as "homes passed" measures potential cable subscribers, telephone customers should be viewed as potential "cable subscribers" via video dialtone or broadband networks. CME/CFA argued that if cable and telephone companies merge, the potential for direct competition in their overlapping areas is removed and smaller video programmers are threatened.[125] CME/CFA further stated that its proposed expansion of the horizontal ownership rules is a logical outgrowth of the "homes passes" standard, as potential VDT subscribers are functionally indistinguishable from potential cable subscribers.[126]

53. MSOs and telephone companies uniformly responded that the Commission does not have the authority under Section 613 to treat telephone customers as "cable subscribers."[127] NCTA and Bell Atlantic argued that Section 613 specifically refers to "cable subscribers" reachable through "cable systems" and that VDT and other systems are

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[125]CME/CFA Petition at 11-13.

[126]CME/CFA Reply at 5-7.

[127]Time Warner Opposition at 9-10; TCI Opposition at 8; Liberty Media Opposition at 12-13; U S West Communications, Inc. Opposition to CME/CFA Petition at 1-3; GTE Service Corporation Opposition to CME/CFA Petition at 2; BellSouth Telecommunications, Inc. Opposition to CME/CFA Petition at 3-7; Bell Atlantic Opposition to CME/CFA Petition at 2-5.

not regarded as "cable services or systems" in their respective proceedings.[128] U S West Communications, Inc. ("U S West") argued that the Communications Act's definition of "cable system" specifically excludes common carrier facilities subject to Title II of the Communications Act.[129] In addition, Bell Atlantic argued that VDT service is not a single "facility" that includes the necessary signal generation, reception and control equipment required of a "cable system," since a VDT network's generation and transmission equipment will generally be provided by the programmers.[130] GTE Service Corporation ("GTE"), BellSouth Telecommunications, Inc. ("BellSouth") and Bell Atlantic also stressed that unlike cable, VDT is an open-access, subscriber controlled system where the subscriber will not be the programming captive of the telephone company, because the telephone company is a common carrier.[131] Liberty Media pointed out that the proposal ignores the Commission's rules prohibiting a telephone company from acquiring a cable system within its telephone service area.[132]

54. Time Warner argued that the CME/CFA proposal would discourage telephone investment in cable and would be fundamentally at odds with the Commission's "two wires" policy.[133] NCTA also stated that CME/CFA's proposition is absurd because it would require the Commission to consider all telephone subscribers as "potential cable customers" in determining the percentages.[134]

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[128]NCTA Opposition at 9-10; Bell Atlantic Opposition at 2-5.

[129]U S West Opposition at 2 (citing 47 U.S.C. § 522(7)).

[130]Bell Atlantic Opposition at 4.

[131]*Id.* at 4-5; GTE Opposition at 2; BellSouth Opposition at 5-7.

[132]Liberty Media Opposition at 12-13 (discussing 47 C.F.R. § 63.54(d)(3)).

[133]Time Warner Opposition at 9-10.

[134]NCTA Opposition at 9-10.

55. Bell Atlantic posited that the proposal would impose an arbitrary limit on the very companies capable of succeeding as new entrants against the cable companies and would provide a disincentive in creating and upgrading VDT services. According to Bell Atlantic, under its then proposed merger with TCI, Bell Atlantic would have upgraded TCI's systems to allow telephone service in competition with incumbent telephone companies. TCI would have divested itself of cable systems in Bell Atlantic's region and Bell Atlantic would have upgraded its networks to compete with these systems. Bell Atlantic noted that similar arrangements were included in other cable-telco transactions proposed at the time the comments were filed.[135]

56. Liberty Media also stated that since the Commission Notices in this docket did not mention potential application of the limits to telephone customers, to extend the limits would violate the Administrative Procedure Act ("APA").[136]

57. CME/CFA responded that the Commission always has the authority to regulate in ways "reasonably ancillary to the effective performance of the Commission's various responsibilities for the regulation of television broadcasting."[137] The Commission has authority under the "reasonably ancillary" test to achieve "long established" goals or "ultimate purposes."[138] CME/CFA asserted that, since the Commission had power before Section 613 to impose horizontal limits

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[135]Bell Atlantic Opposition at 5-8.

[136]Liberty Media Opposition at 12-13 (citing *National Black Media Coalition v. FCC*, 791 F.2d 1016, 1022-23 (2d Cir. 1986) (although final rule need not be an "exact replica of the rule proposed in the Notice," the Notice must be sufficient "to give the public advance notice of the scope of its proceedings")).

[137]CME/CFA Reply at 5-7 (quoting *United States v. Southwestern Cable Co.*, 392 U.S. 157, 178 (1968)).

[138]*Id.* (citing *Home Box Office, Inc. v. FCC*, 567 F.2d 9, 28 (D.C. Cir.), *cert. denied*, 434 U.S. 829 (1977)).

on the cable industry, the Commission certainly has authority to adopt limits which include affiliated telephone subscribers under the "reasonably ancillary" standard.[139] However, CME/CFA stated, that if the Commission finds that considerations of fairness and the APA require further rulemaking, the Commission should initiate such a procedure.

b. Discussion

58. Section 613 specifically authorizes the Commission to place limits on "cable subscribers" a person may reach through "cable systems."[140] Where the use of a telephone company's lines is limited to the provision of local exchange services, we see no reason why that company's telephone subscribers should be counted as cable subscribers for the purposes of the cable horizontal ownership limit.[141] Likewise, the cable horizontal ownership limit does not apply to subscribers of a telephone company that offers multichannel video programming distribution service solely through means other than a "cable system."[142]

59. We note, however, that if a telephone company offers multichannel video programming distribution service to subscribers through a "cable system," the households passed by that cable system would be regarded as "cable households" for purposes of the cable horizontal ownership rules.[143] As discussed below, the Commission

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[139]CME/CFA Reply at 7.

[140]NCTA Opposition at 9-10; Bell Atlantic Opposition at 2.

[141]We note that the proposed TCI-Bell Atlantic merger was never consummated.

[142]*See* 47 U.S.C. § 651 (setting forth options for telephone companies entering the video marketplace). We note that the Commission's VDT rules and policies were repealed by Section 302(b)(3) of the 1996 Telecommunications Act, Pub. L. No. 104-104, 110 Stat. 56.

[143]This standard is consistent with the current horizontal ownership limit, which is based on the cable system's potential reach, i.e., the number of homes

will be seeking further comment on possible revisions to the rules to take into account all MVPD subscribers, such that a person would be allowed to reach fewer subscribers through cable systems if that person also reaches a large percentage of MVPD subscribers nationwide through other MVPD systems, including video distribution by a telephone company.

2. Exemption for Systems Facing Effective Competition

a. Background

60. Bell Atlantic proposed that homes in franchise areas facing "effective competition" not be included in calculating whether an operator has reached the 30% limit.[144] To illustrate Bell Atlantic's proposal, assume that cable company A passed 25% of cable homes nationwide, but 5% of these cable households were in areas subject to "effective competition." Under Bell Atlantic's proposal, if 10% of the cable homes passed nationally were in franchise areas subject to "effective competition," cable company A's horizontal share under the rules would not be 25% but would be 22%.[145] Bell Atlantic argued that horizontal ownership limits are only required to combat the local monopoly and "gatekeeper" power of cable systems, so that the justification for these limits disappear where local distribution markets are

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passed. We note, however, that we are revisiting this issue under the *Further Notice of Rulemaking* and seek comment on the possibility of changing the method of calculating the horizontal ownership limit from potential reach to actual reach, i.e., the number of subscribers served.

[144]Bell Atlantic Petition at 1-2.

[145]To see how this result is reached, assume that 100 million homes are passed nationally, and cable company A serves 25 million of these. If 10% of the nation were in "competitive" markets, the number of households not subject to competition would be 90 million. Cable company A serves 20 million of these, resulting in a percentage of 20/90 or 22%.

competitive.[146]

61. Bell Atlantic argued that subjecting systems under "effective competition" to the horizontal ownership limits will harm competition in the industry. Bell Atlantic contends that, in exempting competitive markets from rate regulation, Congress recognized that competition eliminates the ability of cable operators in those markets to exercise market power and that continued regulatory constraints hinder flexibility in those markets. According to Bell Atlantic, Congress found that cable operators' ability to exercise market power arises from lack of competition in local service areas. As a result, Bell Atlantic asserts, national market power over programmers is diminished by the presence of competition at the local level.[147]

62. CME/CFA argued that Bell Atlantic's argument ignores Congress' well-founded concern that MSOs exercise market power at the national level by dint of sheer size.[148] Congress did not provide an "effective competition" exception here, as it did for rates in Section 3 of the 1992 Cable Act, indicating that Congress did not intend such an exception.[149] CME/CFA noted that Bell Atlantic provides no evidence that the presence of local competition diminishes the incentive or ability of cable operators to favor affiliated programmers and disfavor independents.[150] CME/CFA argued that it is not clear how sporadic local competition seriously undermines the power which flows from "being able to provide ready-made subscriber levels."[151] CME/CFA also pointed out that, because years and "billions of dollars" were

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[146]*Id.* at 2-5.

[147]*Id.* at 1-3, 4-6.

[148]CME/CFA Opposition to Bell Atlantic Petition at 3.

[149]*Id.*

[150]*Id.* at 4.

[151]*Id.* at 6-7.

required before VDT was to become operational, VDT systems at that time could not compete with cable or offer independent programmers a viable alternative to delivery by cable.[152] Since broadcasters are subject to analogous limits despite vigorous competition from local stations, CME/CFA stated that there is no reason for making local competition a basis for dropping the horizontal ownership limits on MSOs.[153]

63. Bell Atlantic responded to the CME/CFA opposition by stressing that it was not asking the Commission to eliminate the ownership limits where only a "theoretical" possibility of competition exists. Instead, Bell Atlantic argued, it simply proposed that these limits not apply where actual head-to-head competition exists. Where competition exists, according to Bell Atlantic, distributors have strong incentives to ensure that consumers obtain the programming they value, regardless of source. The only effect of applying these limits in competitive markets, Bell Atlantic contended, would be to prevent established companies from invading each others' territories and to inhibit entry by those companies that are best equipped to compete with existing MSOs.[154]

b. Discussion

64. We agree with Bell Atlantic that the concern that cable operators may "unfairly imped[e]. . . the flow of video programming from the video programmer to the consumer"[155] will be reduced when there is sufficient competition at the local distribution level. If there is sufficient local distribution competition, the local cable operator will no longer be a "gatekeeper" over that particular audience and video

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[152] *Id.* at 5.

[153] *Id.* at 8-9.

[154] Bell Atlantic Reply at 1-3.

[155] 47 U.S.C. § 533(f)(2)(A).

programmers would have alternative means to reach that audience.[156] We disagree with Bell Atlantic's conclusion that horizontal ownership limits are only required to combat the local monopoly of cable systems, so that the justification for these limits disappears where there is sufficient local competition to satisfy the "effective competition" standard applicable to rate deregulation.

65. A level of competition sufficient to support rate deregulation is not necessarily sufficient to address the public policy objectives of the horizontal ownership rules. As we observed in the *First Order on Reconsideration* in rejecting Bell Atlantic's similar argument in the context of channel occupancy limits, "the effective competition standard was not adopted for this specific purpose and [] it is not clear that the presence of effective competition for any cable system will address all of the relevant concerns that Congress expressed in enacting Section 11 of the 1992 Cable Act."[157] As an example, we noted that, if both the cable system and the competing MVPD are vertically integrated, unaffiliated programming services may continue to be denied access from either outlet, thus frustrating the diversity and competition objectives of the 1992 Act.[158] We agree with CME/CFA that, had Congress intended to eliminate all cable regulations where systems face effective competition, the effective competition exemption would have been drawn much more broadly. Instead, the exemption is expressly limited to rate regulation; nowhere in either its language or legislative history does it state that the presence of head-to-head local distribution competition will render the horizontal ownership rules unnecessary.[159]

66. The "effective competition" standard determines when

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[156] *See Second Report and Order* at ¶ 29.

[157] *First Order on Reconsideration* at ¶ 47.

[158] *Id.*

[159] *Id.* at ¶ 48.

there is sufficient local competition to prevent an incumbent cable operator from exercising market power in setting local rates for cable services sold to local subscribers. In contrast, the horizontal ownership limit was designed to ensure that no cable MSO acquires a sufficiently large share of subscribers nationwide to exercise undue market power at the national level in its purchase of programming from networks, which generally sell their programming nationwide.[160] In the *Second Report and Order*, the Commission rejected an argument similar to that of Bell Atlantic, stating: "The presence of effective competition in any given system or group of systems does not, however, directly respond to Congress' concern about the exercise of undue control by a single entity at the national level."[161] We reaffirm that decision today. We will not assume that, in their bargaining, programming networks and cable MSOs do not consider an MSO's total subscribership, but only its subscribers in areas not subject to "effective competition." There may be grounds for revising the 30% horizontal ownership limit, however, as more systems become subject to effective competition.

3. Attribution Rules

a. Background

67. CME/CFA asked that the Commission tighten its attribution rules by eliminating the single majority shareholder exception, which provides that minority interests will not be attributed where a single shareholder owns more than 50% of the outstanding voting stock.[162] CME/CFA argued that this exception to the attribution rules is "unduly mechanistic" and ignores the minority shareholder's "ability to influence the actual operation of the property" even when a majority shareholder is present. CME/CFA posited that there

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[160]*See Second Report and Order* at ¶ 29; *see also* 47 U.S.C. §§ 533(f)(2)(A), (B) & (C).

[161]*Id.*

[162]CME/CFA Petition at 22-23 (incorporating by reference CFA's September 1993 Reply Comments at 4-5).

are situations where a single majority shareholder may be forced to accommodate minority shareholders.

68. Responding to the CME/CFA proposal, NCTA noted that the attribution rules address the ability of an MSO to influence in a meaningful way the programming decisions of an individual cable system. NCTA argued that the single majority shareholder exception appropriately recognizes that the influence of non-majority shareholders is significantly attenuated when a majority shareholder exists, such that attribution is not required.[163]

b. Discussion

69. In the *Second Report and Order*, the Commission adopted the broadcast attribution rules, which contain the single majority shareholder exception,[164] in the cable horizontal ownership context because "the objectives of the broadcast attribution model are consistent with our goals in establishing ownership standards for subscriber limits."[165] The Commission explicitly stated that the broadcast rules "focus on ownership thresholds that enable a broadcast licensee to influence or control management or programming decisions" and that "these same issues are also relevant to addressing the concerns at issue in this proceeding relating to the ability of cable operators to unduly influence the programming marketplace.[166]

70. The Commission does not believe there is enough evidence in this docket to justify reversing our prior opinion that, in single majority shareholder situations, ownership of minority voting stock alone is unlikely to grant sufficient "influence" over programming decisions to warrant attribution. The single majority shareholder provision of the rules is currently under review in the broadcast

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[163]NCTA Opposition at 15-16.

[164]47 C.F.R. § 73.3555 n. 2(b).

[165]*Second Report and Order* at ¶ 35.

[166]*Id.* at ¶ 35.

context in MM Docket Nos. 94-150, 92-51 and 87-154.[167] In that proceeding, the Commission sought comment on the nature of "influence" and "control" and the connection between equity ownership and such influence and control. The Commission is also issuing a Notice of Proposed Rulemaking seeking comment on whether and how the cable attribution rules should be revised. Given the paucity of information in this proceeding from which to make an informed decision as to the need for changes in the attribution standards, that appears to be the preferable course.

71. This determination regarding the cable attribution rules applies to both our horizontal ownership rules and channel occupancy limits. As we noted in the *First Order on Reconsideration*,[168] that order addressed the issues on reconsideration regarding our cable channel occupancy limits, but left issues concerning the cable attribution standard for the current proceeding.

IV. MOTION TO LIFT STAY

a. Background

72. In the *Second Report and Order*, the Commission voluntarily stayed the effective date of the cable horizontal ownership rules pending final judicial resolution of the District Court decision in *Daniels* that the underlying statute violates the First Amendment.[169] While the *Daniels* Court had stayed further District Court proceedings

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[167] *See Notice of Proposed Rulemaking, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Review of the Commission's Cable Attribution Rules*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 94-324, 10 FCC Rcd 3606 (1995); *Further Notice of Proposed Rule Making, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Review of the Commission's Cable Attribution Rules*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 96-436, 11 FCC Rcd 19895 (1996).

[168] *Memorandum Opinion and Order on Reconsideration of the Second Report and Order* in MM Docket 92-264, FCC 95-147, 10 FCC Rcd 7364, n. 3 (1995).

[169] *Second Report and Order* at ¶ 109.

pending interlocutory appeal of its judgment, it had not enjoined the Commission from adopting and enforcing horizontal ownership rules under the statute.[170] CME/CFA filed a motion to lift the Commission's voluntary stay, which was opposed by NCTA.[171]

73. CME/CFA argued that, because the *Daniels* Court elected to stay further District Court proceedings pending appeal, the Commission's stay "cancels out the Court's stay, resulting in a situation where there are no regulations controlling the growth of cable systems while the constitutionality of the limits is being appealed."[172] As a result, CME/CFA argued, while stays are generally granted to preserve the status quo, the Commission's stay does not preserve the status quo.[173] CME/CFA further argued: (1) that the Commission and the United States are likely to prevail on the merits on appeal;[174] (2) that lifting the stay during the litigation will not result in irreparable harm to cable operators because the current rule still allows expansion for all cable systems and only causes "a temporary inability to expand beyond the 30% limit;"[175] (3) that continuance of the stay could result in harm to video programmers and the public;[176] and (4) that the public interest in "achieving competition and diversity in the cable television marketplace" requires that the rules be enforced while the constitutionality of the limits are under review.[177]

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[170] *Daniels*, 835 F.Supp. at 12.

[171] CME/CFA Motion to Lift Stay; NCTA Opposition to Motion to Lift Stay.

[172] CME/CFA Motion to Lift Stay at 1-2.

[173] *Id.* at 2.

[174] *Id.* at 2-4.

[175] *Id.* at 4.

[176] *Id.* at 4-6.

[177] *Id.* at 6.

74. In its opposition, NCTA argued that the case for a stay is one of "surpassing strength." NCTA stated: (1) that it is "far from clear" that the cable horizontal ownership limits will be upheld; (2) that "irreparable injury will result if cable systems are prevented from lawfully expanding their operations;" (3) that continuance of the stay during the litigation will not harm other interested parties, such as video programmers and the public; and (4) that the public interest favors the stay because the stay avoids "potential confusion and uncertainty during the period of judicial review."[178]

b. Discussion

75. In August 1996, the D.C. Circuit Court consolidated the *Daniels* appeal regarding the facial validity of the statute and the *Time Warner* challenge to the Commission's rules, and determined to hold court proceedings in abeyance while the Commission reconsidered the horizontal rules.[179] In light of the continuing pendency of the judicial proceedings relating to the underlying provision, we will retain the voluntary stay of the 30% horizontal ownership limit at this time.[180] That decision has been appealed and the Commission has argued that the provision in question is indeed constitutional.

76. In order to facilitate monitoring of MSOs' ownership interests, we will lift the stay insofar as it applies to the information submission provisions of 47 C.F.R. § 76.503(c) that are applicable when any person or entity holding an attributable interest in cable systems reaching 20% or more of homes passed nationwide acquires additional

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[178]NCTA Opposition to Motion to Lift Stay at 3.

[179]*Time Warner*, 93 F.3d at 979-80.

[180]Consumers Union/CFA filed a petition for rulemaking on September 23, 1997, requesting, among other things, that the Commission lift its voluntary stay. *Petition to Update Cable Television Regulations and Freeze Existing Cable Television Rates*, RM-9167, MM Docket Nos. 92-264, 92-265, 92-266, at 14-15 (filed Sept. 23, 1997) ("CU/CFA Petition for Rulemaking"). This *Second Order on Reconsideration* denies that particular request.

cable systems. The existing rules require a certification that no violation of the 30% limit will occur as a result of such acquisition. In light of the continuation of the stay, however, the certification should only specify the incremental change the acquisition makes in terms of the 30% of household passed standard, i.e. specifying the ownership in terms of homes passed before and after the acquisition is complete.

77. Affected parties will be required to come into compliance with the horizontal ownership rules within 60 days of the appellate court's issue of a mandate upholding Section 613(f)(1)(a) and the rules, unless the Commission determines as part of this ongoing proceeding to lift the stay at an earlier date. Interested parties, including in particular parties that are now entering into business arrangements that would violate the rules but for the existence of the stay, should be well aware of the existence of the rules and thus have a full opportunity to be prepared to comply with them.

V. FURTHER NOTICE OF PROPOSED RULEMAKING

78. We stated in the *Second Report and Order*, adopting the rules in question in this proceeding, that

> we plan to review subscriber limits every five years to determine whether such limits are reasonable under the prevailing market conditions and whether such limits continue to serve the objectives for which they were adopted. We regard such periodic review as an important means of addressing Congress' intent that such rules reflect the "dynamic nature of the communications marketplace."[181]

The rules in question were adopted in 1993, and it is appropriate that we undertake this review to address intervening changes in the communications marketplace. We seek comment on whether 30% remains the appropriate horizontal ownership limit in light of evolving market conditions. In addition, the current rules allow ownership of additional cable systems reaching up to 35% of cable homes passed, pro-

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[181] *Second Report and Order* at ¶ 40 (citing 47 U.S.C. § 533(f)(2)(E)).

vided such additional cable systems are minority-controlled.[182] The purpose of the minority-control allowance was to encourage diversity of viewpoints by fostering increased minority participation and ownership in the cable industry, through increased MSO investment in minority-owned cable systems.[183] Recognizing that the minority-control allowance has never been utilitized by any MSO, we seek comment on the effectiveness of this rule and on the development of alternative rules to serve our purpose of promoting minority participation. We also recognize that, since this rule was adopted, the Supreme Court issued *Adarand Constructors, Inc. v. Pena*, 515 U.S. 200 (1995). We seek comment on the constitutionality of the minority-control allowance in light of that decision. We also seek comment on how we can develop our policies consistent with the standards set forth in *Adarand*.

79. We also seek comment on two specific issues concerning the method of ownership calculation: (1) whether the rules should consider the presence in the market of all MVPDs rather than cable operators alone, and (2) whether the rules should be based on actual subscriber numbers rather than on homes passed.[184] The rules proposed here would provide that, in calculating a cable MSO's market share, the numerator would consist of the MSO's cable subscribers plus its non-cable MVPD subscribers, and the denominator would consist of the total number of cable subscribers plus non-cable MVPD subscribers nationwide. In addition to these proposed rule changes, we seek comment as to whether the method of ownership calculation should

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[182] 47 C.F.R. § 76.503(b).

[183] *Second Report and Order* at ¶ 28.

[184] The Commission also has issued a *Notice of Proposed Rulemaking, In the Matter of Streamlining of the Commission's Rules for the Direct Broadcast Satellite Service*, FCC 98-26, IB Docket No. 98-21 (rel. Feb. 26, 1998), requesting comment as to whether limitations on cable/DBS cross-ownership are necessary to address horizontal concentration in the MVPD market.

be modified in some way to support cable overbuild competition.

80. The MVPD market has continued to evolve since our adoption of the horizontal ownership rules. The *1997 Competition Report* noted the growth of MVPDs other than cable operators and suggested that a true measure of horizontal concentration ought to take into account all MVPDs and MVPD subscribers, rather than cable operators and cable subscribers alone:

> [I]n assessing the impact that national concentration may have in the MVPD programming market, we believe that it is appropriate to consider the presence of all MVPDs and MVPD subscribers in national concentration figures, and not just cable MSOs and cable subscribers. As non-cable MVPD subscribership increases, the significance of DBS, MMDS and SMATV operators in the MVPD program purchasing market also increases.[185]

With the growth of alternative MVPDs, network programmers gain alternative avenues for distribution of their products, thus reducing cable operators' market power or influence in the purchase and distribution of network programming. Conversely, just as growth in alternative MVPDs' subscribership can reduce a cable MSO's market power, a cable MSO also can increase its market power by acquiring interests in alternative MVPDs.

81. We seek comment on a proposal to revise the rules to include alternative MVPDs in the measure of horizontal concentration in order to reflect the emergence of competitors to cable in the video marketplace, as well as potential MSO increases in market power through acquisition of interests in other MVPDs. By recognizing the impact of all purchasers of video programming, not just cable operators, this rule revision would provide a more accurate measure of MSOs' market power.

82. We seek comment on whether the proposed revision of

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[185] *1997 Competition Report* at ¶ 150.

the horizontal ownership rules is consistent with the Commission's authority under Section 613 of the Communications Act to "prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems . . .."[186] This proposal would result in a sliding or adjustable cable horizontal ownership limit, under which the number of subscribers a cable operator is authorized to reach through cable systems would decrease in proportion with any increase in the number of subscribers that entity reaches through other MVPD systems. Conversely, the cable horizontal ownership limit would rise for a cable operator that reaches fewer subscribers through other MVPD systems. The proposed rules would impose no limit on the number of subscribers a cable operator may reach through alternative MVPD systems. These rules also would not apply to persons who have no attributable ownership interests in cable systems. We seek comment on this proposal and on whether it is consistent with the terms of the underlying statute, given Section 613's focus on the cable industry and the establishment of a cable subscribership limit rather than an MVPD subscribership limit.

83. We also seek comment on the possibility of changing the method of calculating the basis of the horizontal ownership limits from potential reach, i.e., number of homes passed, to actual reach, i.e., number of MVPD subscribers served. In the *Second Report and Order*, we stated that the homes passed standard reflects a cable operator's potential reach and constitutes a more stable basis on which to impose horizontal limits than a subscriber based standard.[187] We also noted some commenters' argument that a subscriber based standard may have the effect of discouraging subscriber growth.[188] In revisiting the horizontal ownership rules, we seek comment on whether the homes

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[186]47 U.S.C. § 533(f)(1)(A).

[187]*Id.* at ¶ 24.

[188]*Id.* at ¶ 19.

passed standard continues to be an accurate measure of horizontal concentration and market power in today's marketplace, and whether the easier to measure subscriber standard can be adapted for use in a fashion that will not require an abrupt halt to the addition of new subscribers to established cable systems.

84. While homes passed reflect the number of subscribers an MVPD has the potential of reaching, the MVPD often secures only a fraction of those potential subscribers. The MVPD typically does not purchase programming for all potential subscribers, only for those subscribers that it actually has. As alternative MVPDs continue to grow in the future, the number of homes passed by a cable operator may become an increasingly inaccurate measure of its actual subscribership and thus of its actual market power. We seek comment on whether the ownership calculation should be based on the number of actual subscribers, rather than homes passed, in order to reflect an MVPD's actual purchasing power.

85. The homes passed standard is also difficult to apply if we revise the horizontal ownership rules to consider all MVPDs in the calculation, since several different MVPDs may pass the same homes. Furthermore, the homes passed standard is a particularly inaccurate measure of market power for a new MVPD whose actual subscribership is only a small fraction of its potential reach in terms of homes passed. For example, under a homes passed standard, each direct to home satellite service provider, no matter how weak or new an entrant, could be deemed to pass virtually all homes in the country and thus be deemed to have far greater market power than an established cable operator passing 30% of homes nationwide. We ask commenters to comment on the best method for counting subscribers, including those residing in multi-dwelling units and commercial subscribers such as hotels, bars, etc.

86. We seek comment on whether the greater accuracy provided by a subscriber based standard outweighs the greater stabil-

ity provided by a homes passed standard. With regard to the argument that a subscriber based standard may have the effect of discouraging subscriber growth, we seek comment on whether system operators would have a sufficient opportunity to anticipate the approaching limit and to dispose of systems sufficient to stay under the limit rather than to simply cease the addition of new subscribers.

87. We ask commenters to address whether these proposed revisions will serve the public interest objectives that Congress directed the Commission to consider and balance in implementing the horizontal ownership limits, particularly the objectives "to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer;"[189] "to ensure that cable operators do not favor affiliated video programmers in determining carriage . . .;"[190] "to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise . . .;"[191] and "to make rules and regulations that reflect the dynamic nature of the communications marketplace."[192]

88. We ask commenters to address whether the proposed revisions are consistent with the Commission's legal authority under Section 613 and other provisions of the Act[193] and are reasonable and appropriate given our objectives. We seek comment on whether the proposed horizontal ownership rules would provide a more accurate measure of horizontal concentration and market power than the current rules. We also seek comment on the practical impact of the

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[189]47 U.S.C. § 533(f)(2)(A).

[190]47 U.S.C. § 533(f)(2)(A).

[191]47 U.S.C. § 533(f)(2)(C).

[192]47 U.S.C. § 533(f)(2)(E).

[193]*See, e.g.*, 47 U.S.C. §§ 151, 154, and 303.

proposed rule changes on MSO ownership and operation. In particular, we ask that commenters address whether the proposed changes would place any cable MSO in violation of the 30% horizontal ownership limit and to provide specific factual information in support of any such conclusions. We seek comment on whether we should develop special rules to address situations where a cable MSO may exceed the 30% limit as a result of subscriber growth within an existing area of homes passed. We further invite comment on any other matters relevant to our proposals and tentative conclusions.

VI. INITIAL REGULATORY FLEXIBILITY ANALYSIS

89. As required by Section 603 of the Regulatory Flexibility Act, 5 U.S.C. § 603 ("RFA"), the Commission is incorporating an Initial Regulatory Flexibility Analysis ("IRFA") of the expected impact on small entities of any policies or proposals contained in this *Further Notice of Proposed Rulemaking* ("*Further Notice*"). Written public comments concerning the effect of the proposals in the *Further Notice*, including the IRFA, on small businesses are requested. Comments must be identified as responses to the IRFA and must be filed by the deadlines for the submission of comments in this proceeding. The Secretary shall send a copy of this *Further Notice*, including the IRFA, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act.[194] In addition, this *Notice* and IRFA will be published in the Federal Register.[195]

A. Need for, and Objectives of, the Proposed Rules

90. The 1992 Cable Act and subsequent actions to implement it, and Section 11(c) of the 1992 Cable Act in particular, are intended to encourage competition in the cable industry and prevent the exercise of undue market power by large cable multiple systems owners. The Commission issues this *Further Notice* to obtain comment

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194 5 U.S.C. § 603(a).

195 *See id.*

on whether certain aspects of the Commission's horizontal ownership rules should be revised to make them more effective in serving the public interest objectives Congress charged the Commission with protecting in Section 11(c).

B. Legal Basis

91. Authority for the actions proposed in this *Further Notice* may be found in Sections 1, 4, 303, and 613 of the Communications Act of 1934, *as amended*, 47 U.S.C. §§ 151, 154, 303, 533.

C. Description and Estimate of the Number of Small Entities to Which the Proposed Rules Will Apply

92. The RFA generally defines "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction" and "the same meaning as the term 'small business concern' under the Small Business Act unless the Commission has developed one or more definitions that are appropriate for its activities.[196] A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration ("SBA").[197] Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency after consultation with the Office of Advocacy of the SBA and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register."[198]

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196 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 15 U.S.C. § 632).

197 15 U.S.C. § 632.

198 While we tentatively believe that the SBA's definition of "small business" greatly overstates the number of cable entities that are small businesses and is not suitable for purposes of determining the impact of any proposals on small cable entities, for purposes of this *Notice*, we utilize the SBA's definition in determining the number of small businesses to which

93. The SBA has developed a definition of small entities for cable and other pay television services under Standard Industrial Classification 4841 (SIC 4841), which covers subscription television services, which includes all such companies with annual gross revenues of $11 million or less.[199] This definition includes cable systems operators, closed circuit television services, direct broadcast satellite services, multipoint distribution systems, satellite master antenna systems and subscription television services. According to the Census Bureau, there were 1,323 such cable and other pay television services generating less than $11 million in revenue that were in operation for at least one year at the end of 1992.[200]

94. The Commission has developed its own definition of a "small cable company" and "small system" for the purposes of rate regulation. Under the Commission's rules, a "small cable company," is one serving fewer than 400,000 subscribers nationwide.[201] Based on our most recent information, we estimate that there were 1,439 cable

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proposed rules would apply. However, we reserve the right to adopt a more suitable definition of "small business" as applied to cable or other entities subject to our rules, and to further consider in the future the number of existing small cable entities.

199 13 C.F.R. §121.201.

200 1992 Census, *supra*, at Firm Size 1-123. *See Memorandum Opinion and Order and Notice of Proposed Rule Making, Implementation of Sections of the Cable Telecommunications Consumer Protection and Competition Act of 1992, Rate Regulation and Cable Pricing Flexibility,* MM Docket No. 92-266 and CS Docket No. 96-157, 11 FCC Rcd 9517, 9531 (1996).

201 47 C.F.R. § 76.901(e). The Commission developed this definition based on its determinations that a small cable company is one with annual revenues of $100 million or less. *Sixth Report and Order and Eleventh Order on Reconsideration, Implementation of Sections of the 1992 Cable Act: Rate Regulation,* MM Docket Nos. 92-266 & 93-215, 10 FCC Rcd 7393 (1995).

companies that qualified as small cable companies at the end of 1995.[202] Since then, some of those companies may have grown to serve over 400,000 subscribers, and others may have been involved in transactions that caused them to be combined with other cable companies. Consequently, we estimate that there are fewer than 1,439 small entity cable companies that may be affected by the proposal adopted in this *Notice*. The Commission's rules also define a "small system," for the purposes of cable rate regulation, as a cable system with 15,000 or fewer subscribers.[203] We do not request nor do we collect information concerning cable systems serving 15,000 or fewer subscribers and thus are unable to estimate at this time the number of small cable systems nationwide.

95. The Communications Act also contains a definition of a "small cable operator," which is "a cable operator that, directly or through an affiliate, serves in the aggregate fewer than 1 percent of all subscribers in the United States and is not affiliated with any entity or entities whose gross annual revenues in the aggregate exceed $250,000,000."[204] The Commission has determined that there are 61,700,000 subscribers in the United States. Therefore, we found that an operator serving fewer than 617,000 subscribers is deemed a small operator, if its annual revenues, when combined with the total annual revenues of all of its affiliates, do not exceed $250 million in the aggregate.[205] Based on available data, we find that the number of cable operators serving 617,000 subscribers or less totals 1,450.[206] Although

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202 Paul Kagan Associates, Inc., *Cable TV Investor*, Feb. 29, 1996 (based on figures for Dec. 30, 1995).

203 47 C.F.R. § 76.901(c).

204 47 U.S.C. § 543(m)(2).

205 47 C.F.R. § 76.1403(b).

206 Paul Kagan Associates, Inc., *Cable TV Investor*, Feb. 29, 1996 (based on figures for Dec. 30, 1995).

it seems certain that some of these cable system operators are affiliated with entities whose gross annual revenues exceed $250,000,000, we are unable at this time to estimate with greater precision the number of cable system operators that would qualify as small cable operators under the definition in the Communications Act. We are likewise unable to estimate the number of these small cable operators that serve 50,000 or fewer subscribers in a franchise area.

D. Description of Projected Recording, Record keeping, and Other Compliance Requirements

96. If our horizontal ownership rules are changed, the Commission may have to change certain cable reporting requirements. Cable entities also may have to adjust the organization of their business interests in order to comply with any new rules that we may adopt.

E. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered

97. The actions proposed in the *Further Notice* are intended to ensure that the Commission's horizontal ownership rules are effective in preventing the exercise of undue market power by large cable multiple systems owners and promote a competitive, diverse and fair marketplace. Accordingly, as discussed in the above descriptions of the proposed rule changes, the approaches proposed in this *Further Notice* should promote fairness and diversity for all cable systems, including the small entities listed above. We invite comments on these approaches, including comment on whether alternative approaches will mitigate any unwarranted expenses incurred by smaller entities by virtue of their size alone.

F. Federal Rules that Overlap, Duplicate or Conflict with the Proposed Rules

98. None.

VII. PAPERWORK REDUCTION ACT

99. The proposals contained herein in the *Further Notice* have been analyzed with respect to the Paperwork Reduction Act of 1995 (the "1995 Act") and found to impose modified information collection requirements. Implementation of any new or modified

requirements will be subject to approval by the Office of Management and Budget ("OMB"). The Commission, as part of its continuing effort to reduce paperwork burdens, invites the general public to take this opportunity to comment on the information collection requirements contained in this *Further Notice*, as required by the 1995 Act. Comments should address: (1) whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (2) the accuracy of the Commission's burden estimates; (3) ways to enhance the quality, utility, and clarity of the information collected; and (4) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology.

100. Written comments by the public on the modified information collection requirements are due 45 days from date of publication of this *Second Order on Reconsideration and Further Notice* in the Federal Register. OMB comments are due 60 days from the date of publication in the Federal Register. Comments on the information collection requirements contained herein should be submitted to Judy Boley, Federal Communications Commission, Room 234, 1919 M Street, N.W., Washington, DC 20554, or via the Internet to jboley@fcc.gov and to Timothy Fain, OMB Desk Officer, 10236 NEOB, 725 - 17th Street, N.W., Washington, DC 20503 or via the Internet to fain_t@al.eop.gov. For additional information on the information collection requirements, contact Judy Boley at 202-418-0214 or via the Internet at the above address.

VIII. PROCEDURAL PROVISIONS

101. *Ex parte Rules - "Permit-but-Disclose" Proceeding*. This proceeding will be treated as a "permit-but-disclose" proceeding subject to the "permit-but-disclose" requirements under Section 1.1206(b) of the rules.[207] Ex parte presentations are permissible if disclosed in accordance with Commission rules, except during the Sunshine Agen-

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[207] 47 C.F.R. § 1.1206(b), as revised.

da period when presentations, ex parte or otherwise, are generally prohibited. Persons making oral ex parte presentations are reminded that a memorandum summarizing a presentation must contain a summary of the substance of the presentation and not merely a listing of the subjects discussed. More than a one or two sentence description of the views and arguments presented is generally required.[208] Additional rules pertaining to oral and written presentations are set forth in Section 1.1206(b).[209]

102. *Filing of Comments and Reply Comments.* Pursuant to applicable procedures set forth in Sections 1.415 and 1.419 of the Commission's Rules,[210] comments are due August 14, 1998, and reply comments are due September 3, 1998. To file formally in this proceeding, you must file an original plus four copies of all comments, reply comments, and supporting comments. If you want each Commissioner to receive a personal copy of your comments, you must file an original plus nine copies. You should send comments and reply comments to Office of the Secretary, Federal Communications Commission, 1919 M Street, NW, Washington, DC 20554. Comments and reply comments will be available for public inspection during regular business hours in the FCC Reference Center, Room 239, Federal Communications Commission, 1919 M Street NW, Washington DC 20554.

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[208] *See* 47 C.F.R. § 1.1206(b)(2), as revised.

[209] 47 C.F.R. § 1.1206(b).

[210] 47 C.F.R. §§ 1.415 and 1.419.

IX. ORDERING CLAUSES

103. Accordingly, IT IS ORDERED that the petitions for reconsideration filed in this proceeding ARE DENIED.

104. IT IS FURTHER ORDERED that the Motion to Lift Stay filed December 15, 1993 by the Center for Media Education and Consumer Federation of America IS GRANTED as to the Commission's voluntary stay on enforcement of 47 C.F.R. § 76.503(c), and IS DENIED as to the Commission's voluntary stay on enforcement of 47 C.F.R. §§ 76.503(a), (b), (d), (e) and (f).

105. IT IS FURTHER ORDERED that, pursuant to Sections 1, 4, 303 and 613 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, 303 and 533, NOTICE IS HEREBY GIVEN of proposed amendments to the Commission's rules, in accordance with the proposals, discussions and statements of issues in the *Further Notice of Proposed Rulemaking*, and COMMENT IS SOUGHT regarding such proposals, discussions and statements of issues.

106. IT IS FURTHER ORDERED that the Commission SHALL SEND a copy of this *Report and Order and Second Further Notice of Proposed Rulemaking*, including the Initial Regulatory Flexibility Analyses, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

Separate Statement of Commissioner Harold Furchtgott-Roth

In re: Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal Ownership Limits, *Second Memorandum Opinion and Order and Further Notice of Proposed Rulemaking*.

I am pleased that the Commission seeks comment on the constitutionality of the 35% "minority-control allowance," 47 CFR section 76.503(b), for cable subscriber limits. *See supra* at 32. In my view, the constitutionality of this provision in light of intervening judicial decisions – most notably, *Adarand v. Pena*, 515 U.S. 200 (1995) – is, at best, dubious.

Accordingly, while it certainly does no harm to seek comment on the efficacy of this regulation, I believe that such comment is entirely unnecessary and I would not have sought it. If a regulation appears to violate the Constitution, that is all we need to know in order to decide whether to affirm it on reconsideration.

At the outset, I note that the Commission's statutory authority to promulgate the minority-control allowance (or any other race-based cable subscriber limits, for that matter) is scant. Section 613(f)(1)(a), which orders the Commission to set horizontal ownership rules, is *entirely race-neutral*. Its plain language supports no rational inference that Congress intended different subscriber limits to apply to different people based on nothing other than their race:

> "[T]he Commission shall . . . prescribe rules and regulations establishing reasonable limits on the number of cable subscribers *a person* is authorized to reach through cable systems owned by *such person*, or in which *such person* has an attributable interest."

47 U.S.C. section 613(f)(1)(a)(emphasis added).

Nor do the "public interest" factors that Congress outlined make any distinctions between people based on minority or non-minority status. *See id.* section 613(f)(2)(A)-(G). To be sure, one of the factors states that the Commission shall "not impose limitations which would impair the development of diverse and high quality program-

ming." Section 613(f)(2)(G). Congress clearly meant for the Commission to protect cable operators' ability to show a wide variety of choice programming by not setting subscriber limits so low as to dry up concentration-based efficiencies that facilitate costly programming investments. *See* House Report at 43; Senate Report at 33; *see also* 8 FCC Rcd at 8571 (observing that "higher concentration levels enable[] cable companies to take advantage of economies of scale and foster investment in more and better original programming and a wealth of viewing options for consumers"). But there is no indication in the statute, or even its legislative history, that Congress meant for the Commission to view the issue of subscriber limits and varied, quality programming through the historically troubled lens of race.

In short, we simply do not have a clear Congressional directive that the Commission, in setting horizontal limits, make race-based distinctions among cable system owners. Given the weighty constitutional issues that arise whenever government employs such classifications, we should be reluctant to read them into statutes. *See generally United States v. Thirty-Seven Photographs*, 402 U.S. 363, 369 (1971) (statutes should be construed to avoid, not to create, constitutional problems).

II.

Section 76.503(b), which on its face employs racial classifications, raises grave constitutional questions. In particular, *Adarand v. Pena*, 515 U.S.200 (1995), which was decided after the Commission promulgated section 76.503(b), casts substantial doubt upon its constitutionality under the Equal Protection component of the Fifth Amendment.

In *Adarand*, the Supreme Court held that *all* governmental action based on race is subject to strict scrutiny. *Id.* at 226. This standard of review obtains, the Court made clear, whether or not the government's motives can be characterized as "benign." *Id.* at 227. Thus, the use of racial classifications by any governmental actor is now constitutionally permissible only where the measure is narrowly

tailored to serve a compelling government interest. *Id.* at 235.[1]

With respect to the government interest in section 76.503(b), the Supreme Court has never held that diversity of programming -- the Commission's purported goal in adopting the minority-control allowance, *see* 8 FCC Rcd 8565, 8578-79 (1993) -- qualifies as a compelling government interest. *See Lutheran Church-Missouri Synod v. FCC*, No. 97-1116, slip op. at 20-21 (D.C. Cir. April 14, 1998) (observing that in *Metro Broadcasting, Inc. v. FCC*, 497 U.S. 547 (1990), the Court held programming diversity to be an important but not a compelling government interest). There is simply no affirmative authority for the proposition that the interest that has been asserted by the Commission in support of its regulation is legally sufficient under strict scrutiny.[2]

Furthermore, as in other contexts, the Commission's stated goal is something of a moving target. The Second Report & Order adopting the allowance does not explain what the Commission actually intends

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[1]As an initial matter, this regulation plainly requires the government to engage in race-based decisionmaking. In situations where a cable operator has more than 30% but less than 36% of national subscribers, the question whether that person is within legal limits for subscribership depends entirely on the racial identity of those who own or control affiliated systems. Therefore, whatever claims might be advanced with respect to the applicability of *Adarand* to other Commission regulations, *cf. Lutheran Church-Missouri Synod v. FCC*, No. 97-1116, slip op. at 13 (D.C. Cir. April 14, 1998) (summarizing and rejecting argument that FCC's equal employment opportunity rules do not involve race-based decisionmaking), it cannot be maintained that government action under this regulation does not turn expressly and precisely upon considerations of race.

[2]In fact, this legal problem -- *i.e.*, the lack of a compelling government interest -- would arise with respect to any regulation created in order to foster programming diversity. I thus find it hard to see how any horizontal ownership rule intended to advance such a goal could be fashioned under *Adarand*, as the Commission suggests. *See supra* at 32 ("We seek comment on how we can develop our policies consistent with the standards set forth in *Adarand*").

to accomplish when it speaks of promoting "diversity" in cable programming. *Cf. id.* at 19 ("The Commission never defines exactly what it means by 'diverse programming.'"). Of course, were "diversity" defined in a content-specific way, such an interpretation would trigger the First Amendment, as the D.C. Circuit has noted. *See id.* at 19-20 ("Any real content-based definition of the term may well give rise to enormous tensions with the First Amendment.").[3]

With respect to the second step under strict scrutiny, the fit between the means and ends here is loose, if not sloppy. The Commission has stated that the 5% allowance will foster investment in minority-owned cable systems, in turn create more minority ownership, and ultimately result in more minority "viewpoints" in programming. *See* 8 FCC Rcd at 8578-79. But the record in this proceeding is devoid of any evidence to support the Commission's predictive rationale, particularly the assumption that cable system ownership by a person of a certain race will lead to an identifable type of programming content. *Cf. Lutheran Church*, slip op. at 22-23 (faulting Commission, in overturning EEO rules as unconstitutional, for lack of evidence "linking low-level employees [at broadcast stations] to programming content"); *Lamprecht v. FCC*, 958 F.2d 382 (D.C. Cir. 1992) (criticizing Commission, in finding gender preferences in licensing hearings unconstitutional, for lack of evidence of connection between female ownership of broadcast stations and "female programming").

Nor has the Commission made any attempt to explain why a 5% allowance is a more appropriate remedy for the posited diversity problem than a more limited allowance of, say, 3%. To the contrary, the flat 5% of extra passage for minority-controlled systems seems an exceedingly blunt instrument for achieving the Commission's goal

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In contrast to broadcasters, cable operators receive full First Amendment protection with respect to their transmission and selection of programming. *See Turner Broadcasting System, Inc. v. FCC*, 512 U.S. 622, 636-41 (1994). Accordingly, the First Amendment "tensions" referred to in *Lutheran Church*, which involved broadcasting, would be even stronger here.

(even if that goal were a legally compelling one, which, under current precedent, it is not). For instance, I can find no connection in the record between the particular percentage of extra subscribers that minority-controlled companies may serve under this regulation and the degree to which that allowance furthers ownership and programming. The 5% allowance thus appears to be a rigid numerical preference, with no record evidence to support either its necessity or efficacy in relation to the purported goal.

Relatedly, there appears to have been no consideration in this docket of race-neutral alternatives for increasing minority ownership or programming participation, as required under the narrow-tailoring prong of strict scrutiny. *See Adarand*, 500 U.S. at 237-38 (citing *Richmond v. J.A. Croson*, 488 U.S. 469, 507 (1989)). The Commission seems to have approached the use of this explicit racial classification as a foregone conclusion, rather than as an alternative approach after first evaluating the utility of rules that do not draw lines among citizens based on their race. Indeed, in the notices of proposed rulemaking and the order of adoption, the Commission never even broached the possibility of race-neutral rules. *See* 8 FCC Rcd 210, 217 n. 58 (1992); 8 FCC Rcd 6828, 6850-51 (1993); 8 FCC Rcd at 8678-79. This is perhaps understandable given that *Adarand* had not been decided at the time these documents were issued, but that fact does not solve the basic deficiency in this proceeding that now exists under that case.

III.

For the foregoing reasons, governing judicial precedent strongly suggests that section 76.503(b), which literally creates two sets of rules for regulated entities based solely on the racial identity of those who own or control related systems, constitutes a denial of equal protection of the laws. The Commission has failed to articulate either a compelling government interest or to achieve a carefully crafted fit between the means it has chosen and the ends it says it intends to promote. The regulation therefore appears to be, at this juncture, facially unconstitutional.

* * *

As indicated above, I certainly cannot object to my fellow Commissioners asking questions about the practical workings of the rule. The significance of such information, however, pales in comparison to the strong indication under existing caselaw that the regulation is unconstitutional. As the courts have admonished us, "[f]ederal officials are not only bound by the Constitution, they must also take a specific oath to support and defend it." *Meredith Corp. v. FCC*, 809 F.2d 863, 874 (D.C. Cir. 1987). If a regulation appears to be unconstitutional, I believe that is reason enough -- indeed, it is the most important reason that I can imagine -- to eliminate the rule.

PARTIAL DISSENT OF COMMISSIONER GLORIA TRISTANI

In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992 -- Horizontal Ownership Limits, MM Docket No. 92-264

I would have lifted the Commission's voluntary stay on the enforceability of the horizontal ownership rules. In 1993, when the stay was imposed, a stay may have made sense: the largest cable operator, TCI, still controlled significantly less than 30% of cable subscribers nationwide and appellate review of the *Daniels* decision could have been expected well before the horizontal limit was threatened. In the past five years, that situation has changed dramatically. By the middle of 1997, TCI controlled 29.3% of cable subscribers, and with the flurry of deals announced over the last several months, it is clear that TCI has breached, or will soon breach, the 30% limit. Moreover, the anticipated appellate review never happened and may not happen anytime soon -- the D.C. Circuit has been waiting for the Commission to release this reconsideration of our rules before examining the underlying statute's constitutionality.

Under these circumstances, the 30% limit we are reaffirming today may be rendered moot unless the stay is lifted. To the extent that TCI already exceeds the 30% limit, I would identify those cases and address them separately. That task may be difficult, but not nearly as difficult as the situation we will face if TCI's dealmaking continues and a year from now the D.C. Circuit upholds the statute. Then we will face a situation in which the "facts on the ground" may severely hamper our ability to implement the right policy.

I recognize that the majority has put cable operators on notice that they must be prepared to come into compliance within 60 days if our rules are upheld. I am supportive of such an admonishment, but I am not convinced that it will be enforced. I therefore dissent on this part of the item.

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